

**FEDERAL RESERVE BANK
OF NEW YORK**

[Circular No. **10294**]
[April 17, 1989]

EXPEDITED FUNDS AVAILABILITY
— **Policy Statement on Delayed Disbursement
of Teller's and Cashier's Checks**
— **Technical Amendments to Regulation CC**

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

The Board of Governors of the Federal Reserve System has announced the adoption of a policy statement discouraging the delayed disbursement of teller's and cashier's checks, in lieu of adopting final amendments to Regulation CC requiring the restriction of such practices. At the same time, the Board of Governors adopted amendments (largely technical in nature) to Regulation CC and its Official Staff Commentary, which are designed to resolve ambiguities and facilitate compliance with the regulation.

Following are the texts of the Board's press releases on these matters:

Delayed Disbursement

The Federal Reserve Board has issued a policy statement discouraging the delayed disbursement of teller's checks and cashier's checks.

The issuance of the policy statement is in lieu of adopting final amendments to Regulation CC to restrict certain delayed disbursement practices as proposed on June 21, 1988.

Delayed disbursement is the practice of issuing checks that are payable by a bank located in a geographic area such that collection of the checks is generally delayed. This practice increases the time and cost for a depository bank to collect the checks. The effects of delayed disbursement are particularly significant in the case of teller's checks and cashier's checks, which must be accorded next-day availability under the Expedited Funds Availability Act and Regulation CC.

Discussions with the major providers of teller's and cashier's check services indicate that they are willing to make operational changes to speed the collection of checks in the markets they serve.

The Federal Reserve Board will monitor adherence to the policy and delayed disbursement practices in general and, if abuses continue, may reconsider whether formal regulatory action may be warranted.

Technical amendments

The Federal Reserve Board has adopted final amendments to Regulation CC and revisions to its Official Commentary to carry out the provisions of the Expedited Funds Availability Act.

The regulation requires banks to make funds available to their customers within specified times, to disclose their funds availability policies to their customers, and to handle returned checks expeditiously.

The amendments are largely technical in nature, and are designed to resolve ambiguities and facilitate banks' compliance with the regulation.

Printed on the following pages is an excerpt from the *Federal Register* of April 6, regarding the Board's policy statement on delayed disbursement, followed by the text of the statement itself. In addition, enclosed — for depository institutions and others who maintain sets of the Board's regulations — are copies of the amendments to Regulation CC and its Official Staff Commentary. Additional copies of this circular or the enclosures may be obtained from our Circulars Division (Tel. No. 212-720-5215 or 5216).

Questions on these matters may be directed to John F. Sobala, Vice President, Check Processing Function (Tel. No. 212-720-6334).

E. GERALD CORRIGAN,
President.

12 CFR Part 229

[Docket No. R-0639]

Policy Statement—Delayed Disbursement of Teller's Checks and Cashier's Checks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Policy statement.

SUMMARY: The Board is issuing a policy statement regarding the delayed disbursement of teller's checks and cashier's checks consistent with the purpose of the Expedited Funds Availability Act. The policy statement is intended to address abuses of delayed disbursement that may give rise to check float while allowing for legitimate centralized teller's check services.

EFFECTIVE DATE: April 10, 1989.

FOR FURTHER INFORMATION CONTACT: Louise L. Roseman, Assistant Director (202/452-3874), or Gayle Thompson, Program Leader (202/452-2934), Division of Federal Reserve Bank Operations; Oliver Ireland, Associate General Counsel (202/452-3625), or Stephanie Martin, Attorney (202/452-3198), Legal Division; for the hearing impaired only: Telecommunications Device for the Deaf, Earnestine Hill or Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION: The Delayed Disbursement Problem

Delayed disbursement is the practice of issuing checks that are payable by, through, or at a bank¹ located in a geographic area such that collection of the checks is generally delayed. In addition to increasing the time for the collection and return of a check, delayed disbursement often increases the costs to process and transport the check. Delayed disbursement practices not only reduce the efficiency of the check collection system, but may also increase the risk to the depository bank because the delay may result in a check being returned after funds must be made available for withdrawal under the Expedited Funds Availability Act ("Act") and the Board's Regulation CC (12 CFR Part 229).

¹ Regulation CC defines "bank" to include all depository institutions, including commercial banks, savings and loan associations, and credit unions. A depository bank is defined as the first bank to which a check is transferred. A paying bank is a bank by, at, or through which a check is payable and to which it is sent for collection.

Delayed Disbursement of Teller's Checks

Although many classes of checks are subject to delayed disbursement, the effects of delayed disbursement are particularly significant in the case of teller's checks.² Many banks issue teller's checks in lieu of cashier's checks (i.e., checks a bank draws on itself). These banks believe that, due to specialization and economies of scale, certain banks and other service providers can perform the tracking, reconciliation, and payment of teller's checks at a lower cost than the issuing bank would incur by issuing and paying cashier's checks. In addition, in certain cases, based on the location of the paying bank vis-a-vis the issuing banks,³ the issuing bank can accrue float benefits from the delayed disbursement of these checks.⁴

The Act requires a depository bank to provide customers with next-day availability, under specified conditions, for certain checks, including cashier's checks and teller's checks, deposited in transaction accounts. Regulation CC extends this next-day availability requirement to checks drawn on Federal Reserve Banks and Federal Home Loan Banks, because these checks have a low risk of return and are often used as a substitute for teller's checks. Depending on the location of the paying bank, a depository bank may not receive credit for the check by the time funds must be

² Regulation CC defines a "teller's check" as a check provided to a customer of a bank, or acquired from a bank for remittance purposes, that is drawn by the bank and drawn on another bank or payable through or at another bank. For the purposes of the proposed amendments to Regulation CC as well as this policy statement, "teller's check" includes checks drawn on a Federal Reserve Bank or a Federal Home Loan Bank. Regulation CC defines "cashier's check" as a check provided to a customer of a bank, or acquired from a bank for remittance purposes, that is drawn on the bank, is signed by an officer or employee of the bank on behalf of the bank as drawer, and is a direct obligation of the bank.

³ Based on a recent Federal Reserve Bank survey, staff estimates that approximately 80 to 80 percent of teller's and cashier's checks are deposited in a bank that is located in the same state as the issuing bank. Thus, when banks issue teller's checks that are payable at a location distant from the issuing bank, the depository bank is also generally distant from the paying bank.

⁴ In some cases, the issuing bank does not remit funds to the paying bank until the day of presentment. In other cases, the issuing bank remits funds to the paying bank before the check is presented. Such funds may be held in a compensating balance account by the paying bank until the check is presented for payment. Earnings from the compensating balance account may be used to offset fees for teller's check services.

made available to the customer for withdrawal. Thus, the practice of delayed disbursement permits a bank issuing such checks to impose costs, in terms of lost interest, on other banks and to benefit from interest or earnings credits earned on outstanding checks until the checks are presented for collection.

Previous Board Actions

Prior to enactment of the Act, the Board's ability to address delayed disbursement abuses was limited to discouraging such practices through policy statements⁵ and Federal Reserve Bank services, such as the High-Dollar Group Sort program. The Act authorizes the Board to make improvements to the check system to speed the collection and return of checks and, thus, to restrict delayed disbursement practices. Specifically, the Act gives the Board "the responsibility to regulate any aspect of the payment system, including the receipt, payment, collection, or clearing of checks; and any related function of the payment system with respect to checks" (12 U.S.C. 4008(c)(1)). The Act also evidences the Congress' intent to speed the availability of funds to bank depositories and, thus, suggests that a reevaluation of delayed disbursement practices is appropriate.

In December 1987, the Board requested public comment on proposed Regulation CC as well as on proposals for long-term improvements to the check collection system (52 FR 47176, December 11, 1987). A number of commenters on proposed Regulation CC cited the inequity of requiring the depository bank to make the proceeds of certain checks, including teller's checks, available for withdrawal on the business day after deposit if the bank cannot receive credit for the checks by that time. Some commenters recommended that the Board restrict the next-day availability requirement to checks for which the depository bank can receive credit by the next business day. Such a restriction, however, would be inconsistent with the Act.

With respect to longer term improvement in the check collection system, the Board requested comment on how to address delayed disbursement practices and the practice of issuing teller's checks payable in a different check processing region than that of the issuing bank. The majority of comments that addressed this issue

⁵ See policy statements issued by the Board on January 11, 1979 and February 23, 1984.

indicated that the practice of issuing teller's checks payable in a different check processing region should be eliminated. Several other commenters (primarily providers of teller's check services) opposed any regulatory action to limit the location of the paying bank.

After an analysis of the comments, the Board issued for comment in June 1988 a proposed amendment to Regulation CC to restrict certain delayed disbursement practices, with a proposed effective date of April 1, 1989 (53 FR 24093, June 27, 1988). Under the proposal, a bank that issued teller's checks would be required to draw the checks on or designate the checks payable through or at a bank such that a depository bank located in the same community as the issuing bank would generally receive credit for the check as quickly as it would receive credit on a check drawn on the issuing bank.

This proposed "equivalent availability" rule was based on the actual check collection practices of banks in the issuing bank's community. The Board did not believe it was practical to address the cases in which teller's checks are deposited in banks distant from the issuing bank, such that the depository banks are unable to receive next-day credit for the checks, even though the depository banks must make the funds available for withdrawal on the next business day. For those checks deposited in a bank local to the issuing bank, the proposed rule was designed to ensure that depository banks generally would receive credit for the teller's check by the next business day, when the funds must be made available for withdrawal.

Public Comment on Delayed Disbursement Proposal

The Board received over 230 written comments from the public, and Board staff held numerous informal conversations with industry representatives regarding the effects of

the proposal. Over 75 percent of the commenters supported the Board's objective to restrict the delayed disbursement of teller's checks; however, commenters indicated that the proposed rule was unclear and would be difficult to administer. Commenters expressed particular concerns about how issuers of teller's checks and providers of teller's check services could determine whether banks in a given community collected checks such that the availability of the teller's checks would be equivalent to the availability the banks receive on checks drawn on the issuing bank.

As an alternative to the proposal, some commenters suggested that a cutoff hour, such as a Federal Reserve deposit deadline, be established such that a check deposited by the depository bank for collection at or after the cutoff hour would receive next-day credit. Several commenters indicated that a combination of Federal Reserve and correspondent deadlines should be referenced to determine whether an issuing bank could issue teller's checks of a particular service provider. Other commenters suggested that the delayed disbursement problem could be resolved, in large part, by requiring that teller's checks be payable locally, or be encoded with a city routing number if payable nonlocally.⁶

The Board has reviewed the public comments received and has evaluated alternative methods of dealing with the delayed disbursement of teller's checks.

⁶ Commenters also expressed concern regarding the proposed effective date of April 1, 1989. Commenters indicated that the proposed rule would require many banks to replace existing teller's check stock or to change providers of teller's check services, thereby necessitating a longer lead time than that provided in the proposal. In response to these comments, the Board issued a notice that should the Board adopt a rule restricting the delayed disbursement of teller's checks, such a rule would not be effective April 1, 1989, as published in the proposal. (54 FR 5495, February 3, 1989).

It has considered the costs of delayed disbursement on depository banks and the burdens on users of teller's check services that might occur should the Board take regulatory action. The Board believes that by issuing a policy statement it can avoid the rigidity of a regulation and still address the problem of intentional delay in the collection of teller's checks. The effectiveness of the policy statement, however, will depend on the cooperation of teller's check issuers and service providers. Discussions with the major providers of teller's check services indicated that they are willing to make changes that would speed the collection of checks in markets they serve. The Board has received commitments from a number of major teller's check providers to make operational changes that would address in large part the concerns that prompted the Board to propose amendments to Regulation CC to restrict the delayed disbursement of these checks.

The Board favors cooperative solutions that do not require rigid regulations and that demonstrate the industry's willingness to work toward payment system improvements. Therefore, the Board is issuing a policy statement in lieu of adopting a final regulation restricting delayed disbursement practices. The effectiveness of the policy statement, however, will depend on the cooperation of teller's check service providers and issuers of teller's checks. The policy statement will be effective immediately, but the Board recognizes that many banks and service providers will need a longer lead time to comply with the policy. The Board will monitor the industry's adherence to the policy statement and delayed disbursement practices in general and, should abuses continue, will consider formal regulatory action.

In light of the foregoing, the Board is issuing the following policy statement:

Board Policy Statement on Delayed Disbursement of Teller's Checks and Cashier's Checks

Delayed disbursement is the practice of issuing checks that are payable by, through, or at a bank¹ located in a geographic area such that collection of the checks is generally delayed. Although many classes of checks are subject to delayed disbursement, the effects of delayed disbursement are particularly significant in the case of teller's checks.² The delayed disbursement of teller's checks imposes float costs on the depository bank, which must generally make the proceeds of these checks available for withdrawal on the business day following deposit. In addition, delayed disbursement often increases the costs to process and transport these checks.

The Expedited Funds Availability Act ("Act") and Regulation CC (12 CFR Part 229) require a depository bank to provide customers with next-day availability, under specified conditions, for certain checks deposited in transaction accounts, including cashier's checks³ and teller's checks. Depending on the location of the paying bank, a depository bank may not receive credit for the check by the time funds must be made available to the customer for withdrawal. Thus, the practice of delayed disbursement permits a bank issuing such checks to impose costs, in terms of lost interest, on other banks and to benefit from interest or earnings credits earned on outstanding checks until the checks are presented for payment.

The Board recognizes that many banks that issue teller's checks benefit from the specialization and economies of scale of certain banks and other service providers that can perform the tracking, reconciliation, and payment services associated with teller's checks at a lower cost than the issuing bank would incur by issuing and paying cashier's checks. In addressing the delayed disbursement problem, the Board believes that it is desirable to reduce the float created by the issuance of these checks while at the same time minimize the disruption of efficient teller's check services.

As a general matter, the Board believes that a depository bank located in the same community as the bank that issues a teller's check should be able to receive next-day credit for the teller's check. The Board has determined, after review of Federal Reserve collection patterns and deposit deadlines across the country, that depository banks in most areas generally can receive next-day credit for checks that are encoded with a nonlocal city routing number⁴ and presented in a nonlocal Federal Reserve city. For checks that are encoded with a nonlocal RCPC or country routing number and presented in a nonlocal check processing region, credit is generally deferred by one or two days. The Board recognizes, however, that depository banks located on the west coast generally may not be able to receive next-day availability for checks presented in most nonlocal cities. In addition, in other isolated areas of the country, next-day credit is generally not available for any check payable by a nonlocal paying bank. The Board recognizes that banks in these areas may benefit by having access to a centralized teller's check service provider.

The Board believes that banks issuing teller's checks and teller's check service providers should take steps to ensure that delays in the collection and return of teller's checks are kept to a minimum:

¹ Regulation CC defines "bank" to include all depository institutions, including commercial banks, savings and loan associations, and credit unions. A depository bank is defined as the first bank to which a check is transferred. A paying bank is a bank by, at, or through which a check is payable and to which it is sent for collection.

² Regulation CC defines a "teller's check" as a check provided to a customer of a bank, or acquired from a bank for remittance purposes, that is drawn by the bank and drawn on another bank or payable through or at another bank. For the purposes of this policy statement, "teller's check" includes checks drawn on a Federal Reserve Bank or a Federal Home Loan Bank.

³ Regulation CC defines "cashier's check" as a check provided to a customer of a bank, or acquired from a bank for remittance purposes, that is drawn on the bank, is signed by an officer or employee of the bank on behalf of the bank as drawer, and is a direct obligation of the bank.

⁴ These checks are payable by banks located in the same city as a Federal Reserve office. RCPC ("Regional Check Processing Center") checks are payable by banks in areas designated within the territories of Federal Reserve offices but outside Federal Reserve cities. Certain Federal Reserve regions also contain country zones, which are generally more remote from Federal Reserve cities than are RCPC zones.

First, the Board believes that any disbursement practice designed to extend the time needed to collect a teller's check is inappropriate. Although the Board believes that centralized disbursement is economically efficient in some cases, the location of the paying bank should be chosen so as to minimize collection time.

Second, the Board has determined that depositary banks can generally receive credit faster for checks payable by a bank with a city routing number than for checks payable by a bank with an RCPC or country routing number. The Board believes that teller's check service providers that serve issuing banks in check processing regions that are nonlocal to the paying bank should help speed the collection and return of teller's checks by use of a city presentment point and a city routing number in the MICR line of its teller's checks.

Some teller's check service providers confine the scope of their services to a state or other limited geographic area. Because the state or area may be divided into more than one check processing region, such service providers may use a paying bank that is nonlocal to many of their customer banks. In addition, the state or area may contain no Federal Reserve city. The Board recognizes that it may be impractical for such service providers to use a city presentment point.

Third, the Board believes that those teller's check service providers that serve banks nationwide should accept teller's checks at more than one presentment point, particularly those providers that serve west coast banks. For example, a teller's check service provider that uses an east coast paying bank could shorten collection and return times for its California customers by also providing a west coast presentment point for teller's checks.

The Board recognizes that similar delayed disbursement problems arise in connection with cashier's checks, issued by a bank with multistate branches, that depositary banks must send to a central location for payment. The Board believes that the same general guidelines should apply to the disbursement of cashier's checks as apply to teller's checks and will take further action regarding cashier's checks should abusive delayed disbursement practices continue to occur.

The Board will monitor the industry's adherence to the policy statement and delayed disbursement practices in general and, should abuses continue, will consider formal regulatory action.

FRASER

Thursday
April 6, 1989
Vol. No. 54, No. 65
Pp. 13841-13855

Regulation CC; Docket No. R-0649
Amendments to Regulation and
Official Staff Commentary

For this Regulation to be complete, retain:
1) Regulation CC Pamphlet, effective September 1, 1988.
2) Amendments effective October 25, 1988.
3) This slip sheet.

[Enc. Cir. No. 10294]

[Docket No. R-0649; Regulation CC]

Availability of Funds and Collection of Checks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board is adopting a number of amendments to Regulation CC and its Commentary (Appendix E to Regulation CC). The regulation requires banks to make funds available to their customers within specified times, to disclose their funds availability policies to their customers, and to handle returned checks expeditiously. Since the publication of Regulation CC, the Board has received numerous requests from banks and others for clarification of various provisions of the regulation. The Board believes that the changes to Regulation CC and its Official Commentary (Appendix E) respond to many of these questions and will aid banks in understanding and complying with the regulation.

EFFECTIVE DATE: The effective date for the amendment to § 229.2(e) regarding agencies of foreign banks and the amendment to Appendix A is August 10, 1989. All other amendments are effective April 10, 1989.

FOR FURTHER INFORMATION CONTACT: Louise L. Roseman, Assistant Director (202) 452-3874 or Gayle Thompson, Program Leader (202) 452-2934 Division of Federal Reserve Bank Operations; Oliver I. Ireland, Associate General Counsel (202) 452-3625 or Stephanie Martin, Attorney (202) 452-3196, Legal Division; or Thomas J. Noto, Attorney (202) 452-3867, Division of Community and Consumer Affairs. For the hearing impaired *only*, Telecommunications Device for the Deaf, Earnestine Hill or Dorothea Thompson (202) 452-3544.

SUPPLEMENTARY INFORMATION: On May 13, 1988, the Board adopted Regulation CC (12 CFR Part 229) to carry out the provisions of the Expedited Funds Availability Act ("Act") (12 U.S.C. 4001-4010). See 53 FR 19372 (May 27, 1988). The regulation requires banks to make funds available to their customers within specified times, to disclose their funds availability policies to their customers, and to handle returned checks expeditiously. After the publication of Regulation CC, the Board received numerous requests from banks and others for clarification of various provisions of the regulation. In October 1988, the Board proposed changes to

Regulation CC and its Official Commentary (Appendix E) to respond to many of these questions and to aid banks in understanding and complying with the regulation (53 FR 44343, November 2, 1988).

The Board received 63 comments on the proposed amendments. Commenters comprised:

| | |
|------------------------------------|----|
| Commercial banks..... | 26 |
| Bank holding companies..... | 15 |
| Trade associations..... | 10 |
| Savings and loan institutions..... | 4 |
| Clearinghouses..... | 3 |
| Banking service corporations..... | 2 |
| Credit unions..... | 1 |
| Federal Home Loan Banks..... | 1 |
| Law firms..... | 1 |

The final amendments and substantive comments are summarized below.

Section 229.2 (Definitions)

(d) *Available for withdrawal.* The Commentary originally stated that funds are considered to be available for withdrawal even though they cannot be used because they are subject to garnishment, tax levy, or court order restricting disbursements from the account. The Board proposed to revise the Commentary to make it clear that when a bank places a hold on funds set aside as a result of the certification of a check, a check guaranty, purchase of a cashier's check, or similar transaction, the bank has not failed to make funds available for withdrawal.

Two commenters suggested that the Board clarify that funds should be considered available for withdrawal if used by a bank in accordance with its right of set-off or if a bank holds the funds "in an account prior to initiation of a wire transfer." The final revision expands on the proposed language to make it clear that the Commentary's list of reasons is not exhaustive and clarifies that banks are permitted under the regulation to place a hold on funds to cover a check that was certified or purchased and not debit the account until the check is presented for payment.

(e) *Bank.* The Expedited Funds Availability Act's definition of "depository institution" includes "an office, branch, or agency of a foreign bank located in the United States" (12 U.S.C. 4001(12)). The definition of bank in Regulation CC, for purposes of subpart B, originally included only branches of foreign banks as defined in the International Banking Act (12 U.S.C. 3101). In some cases, however, agencies of foreign banks may hold accounts. Accordingly, the Board proposed an amendment to the definition of "bank," for purposes of subpart B, to cover

agencies of foreign banks that are located in the United States. (Agencies of foreign banks are already included in the definition of "bank" for purposes of subpart C.) Offices of foreign banks in the United States that are not branches or agencies are not permitted to hold accounts. No substantive comments were received on this change, and the Board has adopted the amendment as proposed. This amendment will become effective 120 days following its final adoption to provide agencies of foreign banks sufficient time to implement the requirements of subpart B.

In addition, the Act did not include Edge Act corporations, agreement corporations, and commercial lending companies (such as banking companies incorporated under Article XII of the New York Banking Law) under the definition of "depository institution"; consequently, the Board did not subject them to the availability and disclosure requirements of subpart B of Regulation CC. For purposes of subpart C, however, the term "bank" also includes any person engaged in the business of banking, so that the same rules apply to the return of checks by institutions that do not hold "accounts" as apply to institutions that do hold "accounts." Edge Act corporations, agreement corporations, and commercial lending companies pay and return checks and drafts and would generally be considered to be engaged in the business of banking. The Board proposed to revise the Commentary to the definition of "bank" to clarify the status of Edge Act and similar corporations under the regulation. No substantive comments were received on this change, and the Board has adopted the revision as proposed.

(f) *Banking day* and (g) *Business day.* The Commentary to these definitions originally stated that deposits made to an ATM are considered made at the branch holding the account into which the deposit is made for the purpose of determining the day of deposit. The Board believes that it is appropriate to apply this rule to deposits made at off-premise facilities, such as remote depositories and lock boxes, as well as at ATMs. All other deposits should be considered made at the branch at which the deposit is received for purposes of determining the day of deposit. The Board proposed to revise the Commentary accordingly.

Many commenters requested that the Board clarify the interaction of the proposed Commentary to the definitions of "banking day" and "business day" and § 229.19(a). The commenters stated

that it was unclear under the proposed language whether deposits to off-premise facilities would still be considered received in accordance with § 229.19(a). The Board has added language in the final revision to the Commentary to clarify the relationship between the two sections.

(i) *Cashier's check* and (gg) *Teller's check*. Sections 229.2(i) and (gg) of the regulations define "cashier's check" and "teller's check." The Board has received several inquiries as to the types of checks that are included within these definitions. One commenter requested that the Board revise the Commentary to the definition of "teller's check" to include checks drawn by a nonbank and payable through a bank. The Board has clarified that such checks are not considered teller's checks under the Act, and has expanded the Commentary to the definitions of "teller's check" and "cashier's check" to make further clarifications.

(k) *Check*. The Commentary to the definition of "check" originally stated that a credit card draft is not considered a check for purposes of the regulation. The Board proposed to clarify the term "credit card draft" by revising the Commentary to specify that the term includes sales drafts used by merchants or generated by banks but excludes checks that banks provide to their customers as a means of accessing credit lines without the use of credit cards. Two commenters expressed confusion regarding the proposed revision, in particular as to what checks would be excluded as "credit card drafts." The Board has revised the Commentary to eliminate confusion.

(u) *Noncash item*. The definition of noncash item includes an item that would otherwise be a check, except that it has not been preprinted or post-encoded in magnetic ink with the routing number of the paying bank. Under the definition of "paying bank," published by the Board as an interim rule on August 18, 1988 (53 FR 31290) and adopted as a final rule on November 2, 1988 (53 FR 44324), the routing number on certain payable through checks may no longer be that of the paying bank for purposes of subpart B of the regulation. The Board is revising the Commentary to clarify that, in the context of this definition, "paying bank" refers to the paying bank for purposes of subpart C. This amendment clarifies that checks payable through a bank are not noncash items.

(z) *Paying bank*. The definition of "paying bank" originally included the state or unit of general local government

on which a check is drawn. Some states and local governments issue checks drawn on themselves, but designate the checks as payable through or at a bank. The Board proposed to amend the definition of paying bank to provide that a state or unit of general local government is a paying bank only if the check is actually sent to the state or unit of general local government for payment or collection. No substantive comments were received regarding this change, and the Board has adopted the amendment as proposed. The Board has also approved a related amendment, as proposed, to conform the warranty provisions in § 229.34 (a) and (b) to the definition of "paying bank."

(bb) *Qualified Returned Check*. The regulation defines a qualified returned check ("QRC") as one that has been prepared for automated return to the depository bank by placing the check in a carrier envelope or placing a strip on the check and encoding the strip or envelope in magnetic ink. Under § 229.31(a), a returning bank's return deadline is extended by one business day if the returning bank converts a returned check to a QRC.

Under the current regulation, returning banks that might want to use another technology for automating returned check processing may not extend their return deadline when using a methodology other than that defined for a QRC. The Board requested comment on whether a broader definition of QRC is warranted to accommodate different technologies, whether banks would use an alternative method of qualifying returned checks if it were available, whether the number of alternative methodologies allowed should be limited, and whether a returning bank should be permitted to extend its return deadline by the additional day to prepare the returned check for processing using another technology if the returned check had originally been qualified by the paying bank.

Twenty-seven commenters opposed broadening the definition of QRC at this time. The reasons cited were a need for uniformity, a need to adapt to the new return system as it exists before experimenting with new technologies, and the need for careful industry study before implementing alternative means of creating QRCs. Six commenters favored broadening the definition now, but three believed the Board should do so only in "a limited way."

Nineteen commenters opposed and two commenters favored allowing an extra day for a returning bank to qualify a returned check using an alternative technology. Some of those opposed said

they would favor the extra day if an agreement was reached between the interested banks or if it would ultimately speed the return. Most commenters said that they would use a new technology in the future if it is sufficiently studied and tested, cost-efficient, and available to all banks. The final amendment does not expand the definition of QRC nor does it allow an extra day for qualifying a returned check using an alternative technology. The Board will, however, continue to study new technologies and options for speeding the return process and may make further proposals in the future.

In addition, the Board proposed to clarify the Commentary to indicate that QRCs prepared using envelopes preprinted with the return item identifier may conform to the guidelines established in *Specification for the Placement and Location of MICR Printing, X9.13* by the American National Standards Committee on Financial Services (Sept. 8, 1983) ("ANSI guidelines") for the external processing code ("EPC") field for printing the identifier. The ANSI guideline states that the EPC field is located within $\frac{1}{4}$ inch to the left of the routing number, thus allowing the identifier to be in either position 44 or position 45 on preprinted envelopes.

The commenters generally approved of universal standards for carrier strips and envelopes. Several commenters opposed the proposal that the "2" identifier be allowed in either position 44 or 45 because their software is capable of reading position 44 only. Since the publication of the proposed amendment, the Board has learned that the ANSI guidelines regarding the EPC field are in the process of revision. The Board will delay action on this amendment until the new ANSI standards are finalized.

(cc) *Returning bank*. The definition of "returning bank" in Regulation CC originally stated that a returning bank is a collecting bank for purposes of U.C.C. 4-202(1)(e), which specifies a collecting bank's duty to notify its transferor of delays in transit. On further consideration, the Board did not believe that it was necessary for Regulation CC to require that a returning bank notify its transferor of any loss or delay in transit, and therefore the Board proposed to delete this reference from the definition.

One commenter objected to the deletion, stating that the transferor needs the notice for chargeback and monitoring purposes. The Board believes, however, that while such a notice is necessary in the forward

collection process, when collecting banks may be in doubt as to whether the check will be paid, it is not as important in the return process, when payment is generally assured as long as the depository bank is solvent. A returning bank will still be a collecting bank for purposes of U.C.C. 4-202(2), which sets out when a collecting bank's action would be considered to be reasonable, and a returning bank is analogous to a collecting bank for purposes of final settlement. Therefore, the Board is adopting the amendment to the regulation as proposed and has added clarifications to the Commentary accordingly.

(kk) *Unit of general local government.* The Board has been asked whether Indian nations are considered to be units of general local government within the meaning of Regulation CC. The Act provides next-day availability for checks drawn by a unit of general local government. Under the Act, a unit of general local government is defined as any city, country, town, township, parish, village, or other general purpose political subdivision of a state. As Indian nations are not subdivisions of the states, Indian nations are not units of general local government within the meaning of the Act, and the Board consequently proposed a revision to the Commentary to make it clear that Indian nations are not included within the meaning of this term. No substantive comments were received on this revision, and the Board has adopted it as proposed.

Section 229.10 (Next-Day Availability)

Certain check deposits. The Commentary to § 229.10 originally stated that banks are required to provide next-day availability (or two-day availability under § 229.10(c)(2)) for Federal Reserve Bank and Federal Home Loan Bank checks. The Board proposed to revise the Commentary to provide that the next-day and second-day availability requirements apply only to checks that are encoded with a routing number listed in Appendix A to the regulation. Banks generally must rely on the routing number to determine whether these checks are subject to next-day availability because the banks cannot require the use of special deposit slips to identify them. The routing numbers assigned to the Federal Reserve Banks and Federal Home Loan Banks may change from time to time, and the Board does not believe that banks should be held liable for not providing next-day availability for a Federal Reserve Bank or Federal Home Loan Bank check that contains a newly issued routing number

that has not yet been included in Appendix A.

One commenter favored the proposal that a bank should be able to rely on the routing numbers published in Appendix A for giving next-day availability to certain checks, but suggested that Appendix A updates have a delayed effective date to facilitate depository bank programming changes. The Board will update Appendix A periodically to incorporate recently issued Federal Reserve Bank and Federal Home Loan Bank routing numbers and will allow a lead time for banks to update their computer systems before imposing liability. The Board adopted the revision as proposed.

In addition, § 229.13(a) of the regulation requires that depository banks give next-day availability to traveler's checks when they are deposited to new accounts. The Board proposed to add a sentence to the Commentary to § 229.10 that cites this requirement, cross-referencing the new account exception in § 229.13. Several commenters suggested that, to avoid confusion regarding the proposed language, the Commentary should clarify that traveler's checks are "included in the \$5000 aggregation" for next-day availability for new accounts. The Board has redrafted the final revision to the Commentary to make this clarification.

Deposits made to an employee of the depository bank. In most cases,

§ 229.10(c) conditions next-day availability on the check being deposited in person to an employee of the depository bank. Deposits made through the mail or at an ATM or night depository must be made available not later than the second business day after the banking day of deposit. Some questions have been raised about the meaning of the term "in person to an employee of the depository bank," e.g., whether it covers situations where a bank sends a courier to the customer to pick up checks for deposit. The language used by the Act is "deposited in a receiving depository institution which is staffed by individuals employed by such institution" (12 U.S.C. 4002(a)(2)), and the Act defines "receiving depository institution" to mean "the branch of a depository institution or the proprietary ATM in which a check is first deposited" (12 U.S.C. 4001(20)). The Board interprets these provisions as requiring next-day availability only for deposits made to staff of the depository bank at a branch of the bank. Under § 229.10(c)(2), second-day availability would apply to deposits described in

this section that are made at a teller station staffed by a person that is not an employee of the depository bank (e.g. a shared staffed teller facility located in a retail store) and to deposits picked up at the customer's premises by an employee of the depository bank. Accordingly, the Board proposed revisions to this section of the Commentary to make these clarifications. One commenter requested clarification in the Commentary as to the day of deposit for deposits picked up by an employee of the depository bank at the customer's premises. The Board has made this clarification in the final revision and otherwise has adopted the revision as proposed.

Fees for withdrawals. The Commentary to § 229.10(c) originally prohibited a depository bank from imposing a fee on a customer when the customer withdraws funds that must be made available under the regulation but for which the bank has not yet received credit. The Board intended this provision to prevent practices designed to discourage customers from exercising their right to withdraw these funds in accordance with the regulation. Banks have expressed concern, however, that this provision could be interpreted to prohibit the application of account analysis programs commonly used by banks under which earnings credits are computed on the basis of collected balances. The Board believes that such programs are generally adopted for legitimate purposes and not for purposes of evading the requirements of the Act. Because of the difficulties in distinguishing these programs from devices to evade the requirements of the Act, the Board proposed to delete this provision of the Commentary.

Thirteen commenters supported the Board's deletion of this provision, stating that the change will prevent widespread confusion and operating problems throughout the industry. Five commenters opposed the proposal, stating that the deletion would invite abuses of the regulation by depository banks. The Board believes that the difficulties caused by the fee for withdrawal language to legitimate account analysis programs outweighs the danger of abuse of the regulation by depository banks. The final amendment deletes the fee for withdrawal language, but the Board plans to monitor the practices of banks in this area and may consider specific restrictions if it determines that abuses are occurring.

Special deposit slips. The Commentary originally stated that if a bank only provides special deposit slips upon the customer's request, the bank's

tellers must advise customers of the special deposit slips' availability. Because banks indicated that this requirement places a difficult burden on tellers, the Board proposed to delete the reference to the tellers' duties. Some commenters expressed concern that if the Board deleted this reference, customers would be told of the availability of such slips only at the time they receive their initial disclosures. The Board is revising the Commentary to indicate that either tellers can advise customers of the availability of special deposit slips, or the bank may post a notice indicating that special deposit slips are available upon request. The notice may be placed, for example, at teller windows or near or with the lobby notice required under § 229.18(b).

Section 229.11 (Temporary Availability Schedule)

(c) *Nonlocal checks.* Under the temporary schedule, funds deposited by nonlocal check must be made available for withdrawal no later than the seventh business day following the banking day of deposit. The Commentary originally stated that exceptions to this rule include deposits in accounts of banks located outside the 48 contiguous states and deposits made to nonproprietary ATMs. The Board proposed to delete the reference to nonproprietary ATM deposits because § 229.11(d) already requires that all checks deposited at nonproprietary ATMs be made available no later than the seventh business day following the banking day of deposit. No substantive comments were received on this change, and the Board adopted the revision as proposed.

Section 229.13 (Exceptions)

(b) *Large deposits.* Section 229.13(b) permits a depository bank to extend the hold placed on local and nonlocal check deposits to the extent that the aggregate amount of the deposit on any banking day exceeds \$5,000. After the final rule was adopted, several banks asked if there is a rule to determine what portion of a large-dollar deposit that is composed of both local and nonlocal checks should be made available in accordance with the schedule and which checks may be held for a longer period of time under this exception. The Board intended to leave this determination to the discretion of the depository bank, and proposed a revision to the Commentary to clarify this point. No substantive comments were received on this change, and the Board adopted the revision as proposed.

(e)(2) *Overdraft and returned check*

fees. Originally, the last sentence of this paragraph of the regulation stated that "[t]he overdraft and returned check notice must state that the customer may be entitled to a refund of overdraft or returned check fees * * *." This sentence, when read with the notice requirement of § 229.13(g), could have been interpreted to require banks to provide duplicate notices to their customers in certain cases. The Board proposed to amend the last sentence of this paragraph to clarify that only one notice is required. No substantive comments were received on this change, and the Board has adopted the amendment as proposed.

Section 229.16 (Specific Availability Policy Disclosure)

The Board is clarifying two disclosure issues that have been raised since Regulation CC took effect. These clarifications would not require banks to change disclosures that have already been printed or mailed.

(a) *General.* Section 229.16(a) of the regulation requires banks to provide their customers with a specific policy disclosure that reflects the bank's availability policy followed in most cases. The Board proposed two revisions to the Commentary to clarify this provision. First, the Board proposed to clarify that if a bank discloses the policy it follows in most cases, it need not disclose to some customers that they may get faster availability. In addition, the Board proposed to clarify that a bank does not violate the disclosure requirements of the regulation if it pays checks written on an account prior to the day funds in the account become available for withdrawal according to its disclosure. Generally, as long as funds are not available for withdrawal for all uses permitted to the customer, they are not "available for withdrawal" as that term is defined in the regulation and, generally, disclosures based on the time that funds are available for all uses are proper. No substantive comments were received on these changes, and the Board has adopted the revisions as proposed.

(b) *Content of specific availability policy disclosure.* Section 229.16(b) of the regulation describes the required contents of the specific availability policy disclosure. The Board proposed to revise the Commentary to § 229.16(b) to clarify that a bank that provides availability based on when the bank generally receives credit for deposited checks need not disclose the time when a check drawn on each bank will be available for withdrawal. Instead, the Board proposed that the bank may

disclose the categories of deposits that must be available on the first business day after the day of deposit, state the other categories of deposits and the time periods that will be applicable to those deposits, and state that the customer may request a copy of the bank's schedule for when deposits of those checks will be available for withdrawal. No substantive comments were received on this change, and the Board has adopted the revision as proposed.

(c)(3) *Overdraft and returned check fees.* The last sentence of this paragraph of the regulation originally stated that "[t]he overdraft and returned check notice must state that the customer may be entitled to a refund of overdraft or returned check fees * * *." This sentence, when read with the notice requirement in § 229.16(c)(2), could have been interpreted to require banks to provide duplicate notices to their customers in certain cases. The Board proposed to amend the last sentence of this paragraph to read "the notice must state that the customer may be entitled to a refund of overdraft or returned check fees * * *." No substantive comments were received on this change, and the Board has adopted the revision as proposed.

Section 229.19 (Miscellaneous)

(a) *When funds are considered deposited.* This paragraph establishes rules to determine when funds are considered received in various circumstances. Rules applicable to deposits made at staffed teller stations differ from those that apply to deposits made at off-premises facilities, such as lock boxes or night depositories. The Board proposed a revision to the Commentary to clarify that the rules applicable to funds deposited in a deposit box located in the lobby of the bank should be similar to the rules for funds received at a staffed teller station. Seven commenters favored the proposal, stating that the change is reasonable in light of customer expectations but that the Board should clearly distinguish between boxes inside the lobby and boxes attached to the lobby but accessed from outside. Six commenters were opposed, explaining that for security reasons, lobby boxes are not emptied while the lobby is open to the public, and consequently it is impractical to treat those deposits the same as deposits to a teller. One commenter suggested that a notice on the lobby box as to when funds will be considered received would be sufficient. The final revision provides that a lobby box deposit is treated the same as a deposit to a staffed teller station, unless

the bank treats lobby box deposits the same as deposits to night depositories and provides a notice on the lobby box informing customers when deposits at the lobby box will be considered received.

Section 229.19(a)(5)(ii) permits a bank to establish a cut-off hour of 2:00 p.m. or later, after which deposits may be considered made on the following banking day. This provision is similar to U.C.C. 4-107. Recognizing that many banks close before 2:00 p.m., the Commentary notes that this provision does not require banks to stay open until 2:00 p.m. The language in the Commentary raised a number of issues, such as the effect of closing most of the bank but leaving drive-up teller windows open. The Board proposed a revision to the Commentary to clarify the effect of closing practices on cut-off hours. The Board received one comment regarding the provision prohibiting a bank from considering checks accepted at certain teller stations before 2:00 p.m. as the next day's deposits. The commenter stated that prohibiting this practice would hurt many small rural banks that must close their teller windows before 2:00 p.m. to meet courier schedules. The commenter stated that these banks would incur greater risk by losing a day of collection time for those deposits accepted before 2:00 p.m. but after the courier deadline. Regulation CC, however, incorporates the U.C.C.'s existing 2:00 p.m. cut-off hour for over-the-counter deposits, thus these delays already occur. The Board has adopted the final revision as proposed, which reflects current law under the U.C.C.

(e) *Holds on other funds.* Section 229.19(e) of the regulation limits the hold a depository bank may place on any funds of the customer due to a deposit to an account covered by the regulation. For example, for deposits made to a customer's checking account, if a bank places a hold on funds in a nontransaction account, such as certain savings accounts, rather than the customer's checking account, the bank may place such a hold only to the extent that the funds held do not exceed the amount of the deposit and the length of the hold does not exceed the time periods permitted by the regulation. This restriction is intended to prevent evasion of a principal purpose of the Act, i.e., to limit holds on deposits to transaction accounts.

The regulation originally limited holds that a bank can place on funds of the customer if the customer cashes a check over the counter to holds that do not

exceed the time periods prescribed in the regulation and do not exceed the amount of the check cashed. A number of banks argued that, as to checks cashed over the counter, the restriction was overly broad because cashing a check over the counter and placing a hold on a nontransaction account does not involve an "account" covered by the Act.

The Board proposed to amend § 229.19(e) so that, in the case of checks cashed over the counter, the regulation would not limit holds placed on funds that are not held in accounts as defined by the regulation. The comments on the proposal were split, four opposed and three in favor. Those opposed stated that the change was contrary to the spirit of the Act and invites abuses of hold periods. The Board believes, however, that it is inappropriate to regulate holds when there has not been a deposit to or hold on an account covered by Regulation CC. The amendment to § 229.19(e) has been adopted as proposed. The Board has also clarified in the Commentary to § 229.19(e) that a depository bank may not place a hold on any account when an on us check is cashed over the counter, because on us checks are considered finally paid when cashed.

Section 229.20 (Relation to State Law)

The Act (section 608, 12 U.S.C. 4007) provides that any state law in effect on or before September 1, 1989, that provides for a shorter hold for a category of checks than is provided under Federal law will supersede the federal provision. Section 229.20 of the regulation provides for Board determinations, upon request, of whether state law relating to the availability of funds is preempted by Federal law and also provides certain preemption standards.

In August 1988 and October 1988, the Board adopted preemption determinations with respect to the laws of several states. See, for example, 53 FR 32359 (Aug. 24, 1988). In formulating those preemption determinations, the Board adopted certain uniform principles that will apply in all Board preemption determinations. The Board proposed to revise the Commentary to § 229.20 to incorporate these principles for preemption determinations.

One commenter suggested that if a state law provides for the same availability schedules as the Federal law but does not provide for exceptions to the schedules, then the Federal exceptions should apply. The Board believes that, under the Act, such a state law would, in effect, provide for a

shorter hold period than Federal law and would therefore supersede Federal law to the extent that the Federal exceptions provided a longer hold period.

One commenter argued that Federal law should preempt state law when state availability schedules are the same as the Federal schedules, as well as when state schedules are shorter. The Act, however, states that the Federal law shall supersede inconsistent state laws, and the Board believes that state laws that are the same as the Federal law are not inconsistent with the Federal law. The commenter was also of the opinion that under the Act, state law may preempt Federal law only if the state law applies to all federally insured depository institutions within a state; however, the Act provides that if state availability schedules are shorter than the Federal schedules, then the state schedules shall supersede the Federal schedules and shall apply to all federally insured depository institutions located within the state.

Another commenter suggested that because the relationship between State and Federal law is often complicated, the Board should relieve banks from liability due to unintentional noncompliance due to that complex relationship; however, such a revision would be contrary to the Act. The Board has adopted the revisions to this section of the Commentary as proposed.

Section 229.30 (Paying Bank's Responsibility for Return of Checks)

(a) *Return of checks.* Prior to the effective date of Regulation CC, a paying bank usually returned a check to the presenting bank and automatically received a refund of any provisional settlement it may have made. Under Regulation CC, the paying bank must make an expeditious return, which may or may not involve returning the check through the presenting bank. If the paying bank does not return through the presenting bank, it will receive payment for the check from the bank to which the check is returned (a returning bank or the depository bank). In these cases, any credit given to the presenting bank is not charged back.

In rare cases, a paying bank that returns a check may not have settled for the check with the presenting bank. In such cases, if the paying bank returns the check other than through the presenting bank, it should be required to make prompt payment for the amount of the check to the presenting bank. The Board proposed to revise the Commentary to § 229.30(a) to clarify this

point. No substantive comments were received on this change, and the Board has adopted the revision as proposed. In addition, the Board has added a cross-reference to the Commentary to § 229.33(a) regarding a paying bank's duty toward a party that has breached a presentment warranty.

(b) *Unidentifiable depositary bank.* if a paying bank is unable to identify the depositary bank, it may return the check to any bank that handled the check for forward collection, even if that bank has not agreed to act as a returning bank. If a paying bank chooses this option, it must advise the collecting bank that it is unable to identify the depositary bank. The Board proposed to revise the Commentary to provide that this notice must be conspicuous, and that the paying bank may not prepare the check for automated processing.

Nine commenters opposed this proposal, and three specifically supported it. Those opposed stated that if the depositary bank is unidentifiable, the check would be returned faster if the paying or subsequent returning bank were allowed to qualify the returned check with the routing number of the prior collecting bank to which it is being sent (and also signify on the check that the depositary bank is unidentifiable). The commenters stated that, under their approach, the check would not have to be handled manually until it rejected at the prior collecting bank. The Board does not believe that return times would be shorter if the returned checks are qualified to the prior indorser. Further, the Board believes that in some cases such a check would be returned to the depositary bank later than would be the case had the check been handled as a raw return.

Commenters also stated that under the proposal, the paying or returning bank would be charged a higher raw return fee because of another bank's error. Five commenters claimed that **Federal Reserve Banks have been "dumping" returned checks on the prior collecting bank with the clearest indorsement without making a serious effort to identify the depositary bank.** The commenters objected to this practice and were concerned that the liabilities were being shifted from the Reserve Bank to the prior collecting bank. One commenter suggested that the Board establish a procedure by which the cost of handling a returned check for which the depositary bank is unidentifiable is passed along to the bank at fault.

The Board believes that these problems are directly related to the ease

of identifying depositary banks and that the number of returned checks for which the depositary bank is unidentifiable can best be reduced by improving the quality of depositary bank indorsements. The Federal Reserve Banks are currently working with depositary banks with poor-quality indorsements to improve indorsement legibility. The higher costs being imposed on paying banks due to poor depositary bank indorsements should be minimized as indorsement quality improves.

The Board further believes that by keeping unidentifiable depositary bank checks in the raw processing stream, paying and returning banks will have incentives to make additional efforts to identify the depositary bank. Allowing paying or returning banks to qualify returned checks sent to a prior indorser would provide an incentive for the bank to qualify returned checks to the prior indorser to obtain the lowest per item fee rather than to make every effort to identify the depositary bank. In addition, a returning bank may have more familiarity with various depositary bank indorsements and may be able to determine the depositary bank, even when the paying bank is unable to do so. Accordingly, the Board has decided to adopt the proposed revision prohibiting the preparation of returned checks for which the depositary bank is unidentifiable for automated return.

In addition, several commenters asked the Board to define "conspicuous notice." The Board proposed a conspicuous notice requirement so that a bank that receives a returned check will be readily able to distinguish a check for which the depositary bank is unidentifiable from other returned checks. If returned checks for which the depositary bank is unidentifiable are received in a cash letter commingled with other returned checks, conspicuous notice would have to be given on each individual check for which the depositary bank is unidentifiable, for example in the form of a stamp on the check. If returned checks for which the depositary bank is unidentifiable are received in a separate cash letter, only one notice would need to be given for the entire cash letter. The final revisions to the Commentary have been revised accordingly.

Furthermore, the Commentary originally stated that the sending of a check to a bank that handles the check for forward collection under this paragraph, but that has not agreed to handle returned checks expeditiously, is not subject to the requirements for

expeditious return by the paying bank. The Board proposed to delete the phrase "but that has agreed to handle returned checks expeditiously." The duty of expeditious return would not apply when a check for which the depositary bank is unidentifiable is sent to a prior indorser, regardless of whether the prior indorser agrees to handle expeditiously returned checks in general. No substantive comments were received on this change, and the Board has adopted the revision as proposed.

(f) *Notice in lieu of return.* This paragraph originally provided that a paying bank may send a notice of nonpayment in lieu of the physical check if the check is lost or otherwise unavailable. The Board does not believe that a check is unavailable merely because a bank has filed it in a way that makes its retrieval inconvenient or difficult. The Board proposed to clarify that notice in lieu of the return of the actual check should be permitted only when a bank does not have and cannot obtain possession of the check or must retain possession of the check for protest. Several commenters requested that a legible photocopy should be the only allowable form of notice in lieu. Others suggested that notices in lieu could be discouraged by providing that the paying bank send a fee to the depositary bank when it sends a notice in lieu. The Board believes that the current requirements for the content of a notice in lieu provide the depositary bank with sufficient information. The Board recognizes that the cost of processing a notice in lieu can be higher than the cost of processing a returned check and has clarified the limited situations in which a notice in lieu may be sent. The final amendment includes the proposed language and also clarifies that the notice in lieu must be sent in the same manner as other returned checks. The final amendment makes these changes in both §§ 229.30F(f) and 229.31(f).

Section 229.31 (Returning Bank's Responsibility for Return of Checks)

(b) *Unidentifiable depositary bank.* This paragraph provides, among other things, that a returning bank that receives a check from a paying bank that could not identify the depositary bank must return the check expeditiously to the depositary bank if it is able to identify the depositary bank. The Board proposed to amend the regulation to clarify that this requirement also applies to checks that a returning bank receives from another returning bank where the prior returning

bank is not able to identify the depositary bank.

Comments on this section were similar to those on § 229.30(b). One commenter suggested that the Board clarify that a bank must accept returns only if it agrees to handle returns or is the depositary bank or a prior collecting bank. Another commenter suggested that if a prior collecting bank is able to identify the depositary bank by looking at the indorsement (which would indicate that the sender of the check had not made a good faith effort to make the identification), the prior collecting bank should be able to charge the sender a fee. One commenter asked the Board to establish a preferred sequence for where to send a check when the depositary bank is unidentifiable.

Because the comments on the proposed revisions to § 229.31(b) of the regulation generally referenced back to the Board's proposal regarding the Commentary to § 229.30(b), they are discussed above in that section. The proposed changes to § 229.31(b) of the regulation were intended to clarify that the same rules applied to returned checks received from a paying bank and those received from another returning bank. None of the comments directly addressed this issue, and the Board has adopted the amendment as proposed.

In addition, the Board proposed a revision to the Commentary to § 229.31(b). Originally, the Commentary stated that a returning bank may send a check for which the depositary bank is unknown to a returning bank that agrees to handle "the returned check" for expeditious return or to a prior collecting bank, even though the prior collecting bank does not agree to handle "returned checks" expeditiously. The Board proposed to change the phrase "returned checks" to "the returned check" to clarify that a returned check may be sent to a prior collecting bank even though the prior collecting bank does not agree to handle the returned check expeditiously. No substantive comments were received on this change, and the Board has adopted the revision as proposed. In addition, the Board has added clarifying language similar to the language adopted in the Commentary to § 229.30(b) regarding conspicuous notice and the prohibition on qualifying a check for return if the depositary bank is unidentifiable. The Board has also added a cross-reference in the Commentary to § 229.31(c).

Section 229.32 (Depositary Bank's Responsibility for Returned Checks)

Under § 229.32(a)(2), a depositary

bank must accept returned checks at a location consistent with the name and address of the depositary bank in its indorsement on the check, or, if no address appears in the indorsement, at a branch or head office associated with the routing number of the depositary bank in its indorsement. A depositary bank's indorsement could contain an address that is in a different check processing region from an address associated with the routing number in the indorsement. As returned checks will be routed on the basis of the routing number in the depositary bank's indorsement, the return of checks will be facilitated if returns can be made to an address in the same check processing region as the location associated with the routing number. Therefore, the Board proposed to amend § 229.32(a)(2) to provide that if the address in the depositary bank's indorsement is not in the same check processing region as the address associated with the routing number in its indorsement, the depositary bank must accept returned checks at a branch or head office associated with the routing number in the indorsement.

Three commenters opposed the amendment, stating that it would force changes in operating procedures, cause a loss of efficiency, specialization, and economy of scale, and increase confusion and delay. Others suggested that as long as one address is known, it should be sufficient. One commenter supported the amendment only if the address associated with the routing number is a forward presentment receipt site.

The Board has adopted the amendment with slight modification. This amendment would not prevent a bank from centralizing its check processing operations to gain efficiencies and economies of scale. The Board believes that if a bank operating in multiple check processing regions chooses to centralize check processing at one site, then that bank should bear the extra cost of transporting checks to that site. Furthermore, paying banks generally return checks based on the depositary bank's routing number. A paying bank located in the same check processing region as the depositary bank should have the option of sending returned checks to the depositary bank's address that is associated with its routing number in its indorsement, rather than bearing the possibly higher cost of delivery to a nonlocal processing center.

Section 229.32(a) also permits depositary banks to require that

returned checks be sorted separately from forward collection checks. The intent of this provision is to require paying or returning banks to present returned checks to the depositary bank separately sorted from forward collection checks, unless the depositary bank agrees to take returned checks commingled with forward collection checks.

The Board proposed to add similar language to the regulation and Commentary to state that a depositary bank may require returned checks for which it is the depositary bank to be separately sorted from checks for which it is a returning bank, including those for which it is a prior indorser. This amendment was intended to facilitate the handling of checks that are returned to prior indorsers because of difficulty in identifying the depositary bank.

Five commenters opposed requiring separate cash letters for different types of returns. Those who opposed the proposal said that the benefits to the receiving bank were outweighed by the burden on the sending bank and that more errors and longer delays would result. Four commenters explicitly supported the proposal. The Board has found that most banks that receive returned checks both as prior indorser and depositary bank currently receive these checks commingled. The Federal Reserve Banks have received few complaints about the commingled cash letters. Thus, the Board has determined that commingled return cash letters are not causing a problem and that current practices should be allowed to continue. The Board has not adopted the proposed amendment.

The Board also proposed to add a sentence to the Commentary to § 229.32(a) to clarify that, under § 229.33(d), a depositary bank receiving a returned check or notice of nonpayment must notify its customer by its midnight deadline or within a reasonable time. One commenter suggested that the amendment should read "must send notice to its customer" rather than "must notify its customer." The Board has incorporated this suggestion in the final revision.

Section 229.33 (Notice of Nonpayment)

(a) *Requirement.* This section requires a paying bank to give notice of nonpayment to the depositary bank if it determines not to pay a check of \$2,500 or more. The Board proposed a revision to the Commentary to clarify that a paying bank's failure to give notice of nonpayment may be offset by a

depository bank's breach of warranty of title or other warranty regarding a check. One commenter disagreed with the proposal, stating that the paying bank should be responsible for failure to give notice of nonpayment in all instances. One rationale for the commenter's position is that, in some cases, the loss to the depository bank would not occur but for the failure of the paying bank to give timely notice of nonpayment. At least one court has agreed with the commenter's position, interpreting the warranty provisions of U.C.C. 4-207(a)(1) and Regulation J to apply only when a paying bank pays the check and holding that a depository bank's breach of presentment warranty did not absolve the paying bank from liability for failing to give timely notice of nonpayment. (See *First American Savings v. M & I Bank*, 57 U.S.L.W. 2406 (3rd Cir. 1989).)

The Board, however, believes that a paying bank should not be responsible to a depository bank for failure to give notice in a case where the depository bank has breached its warranty, such as where the check has been stolen or an indorsement forged. This position places the loss on the bank closest in the collection chain to party who is responsible for the check (e.g., the person who stole the check or forged the indorsement). Accordingly, the Board has adopted the amendment as proposed and has also added similar wording to the Commentary to § 229.30(a).

(d) *Notification to Customer.* This section requires a depository bank to notify its customer upon receipt of a returned check or notice of nonpayment. The Board has received several requests from banks to clarify whether this duty applies to all returned checks or only to returned checks of \$2,500 or more. The Board is revising the Commentary to clarify that this provision applies in the case of any returned check or notice of nonpayment, regardless of amount.

Sections 229.34 (Warranties by Paying Bank and Returning Bank) and 229.38 (Liability)

The Board proposed several technical amendments that are necessary to accommodate cases where a check is payable by one bank but payable through another. These amendments to §§ 229.34 and 229.38 clarify that in cases of payable through checks payable by a bank, the bank by which the check is payable, not the payable through bank, makes the paying bank's warranties and is liable for the condition of the back of

a check. No substantive comments were received regarding these changes, and the Board is adopting the amendments with slight technical modification.

Section 229.35 (Indorsements)

(a) *Indorsement standards.* The indorsement standard in § 229.35 and Appendix D specifies the information that must be included in a depository bank's indorsement. The standard also permits depository banks to include other identifying information in their indorsements. Some banks have included nine-digit zip codes in their indorsements. The Board believes that the inclusion of the nine-digit zip code could lead paying and returning banks to confuse the zip code with the routing number, which also contains nine digits. In order to prevent this confusion, the Board proposed to amend the Commentary to § 229.35(a) to advise depository banks not to include in their indorsements information, such as a nine-digit zip code, that could be confused with required information, such as the depository bank's routing number. Eight commenters specifically favored the Board's proposal to discourage the use of numbers in depository bank indorsements that could be confused with routing numbers, such as nine-digit zip codes. One commenter opposed the proposal on the grounds that use of the nine-digit zip code will grow over time. Another commenter suggested that any ban on use of nine-digit zip codes should allow a sufficient lead time for implementation. The Board has adopted the amendment as proposed. The Board is not banning the use of nine-digit zip codes in indorsements but is merely discouraging them.

The Board also proposed revisions to the Commentary to § 229.35(a) to reference the amendments to § 229.32(a) and to clarify that the collecting and returning banks must indorse checks for tracing purposes. No substantive comments were received on these changes, and the Board has adopted the revisions as proposed.

(b) *Liability of bank handling check.* This paragraph originally provided that a bank handling a check for forward collection or return may have the rights of a holder. The Board proposed to revise the Commentary to clarify that a bank may become a holder or a holder in due course regardless of whether prior banks have complied with the regulation's indorsement standards. No substantive comments were received regarding this change, and the Board has adopted the revision as proposed and has also added language to this section

clarifying the use of the term "final settlement."

Section 229.37 (Variation by Agreement)

The Commentary to this section notes that the Board did not adopt the rule stated in U.C.C. 4-103(2), which provides that Federal Reserve regulations and operating letters, clearinghouse rules, and the like have the effect of agreements under the U.C.C. that apply to parties that have not specifically assented to them. The Board did not, however, intend to affect the status of such agreements under the U.C.C., and the Board proposed to clarify this point in the Commentary. No substantive comments were received regarding this change, and the Board has adopted the revision as proposed.

Appendix A (Routing Number Guide to Next-Day Availability Checks and Local Checks)

The Board is updating the list of Federal Home Loan Bank routing numbers to include a newly-issued routing number of the Houston Branch of the Federal Home Loan Bank of Dallas.

Appendix C (Model Forms, Clauses and Notices)

Forms C-1 through C-3 disclose that a bank generally provides next-day availability for all funds deposited to an account. Forms C-4 through C-7 list social security benefits and payroll payments as examples of preauthorized credits that are given next-day availability. Under U.S. Treasury regulations, government payroll and benefit preauthorized transfers must be made available on the payment date. ACH association rules encourage banks to make direct deposit of payroll payments available to the customer on the payment date. The Board is adding language in the Appendix C Commentary to the model forms to clarify that banks that have relied on the model forms are protected from civil liability under § 229.21(e) as to disclosure of electronic payments, even though social security benefits and payroll payments are being made available on the same, not the next, business day. Banks are encouraged to revise their forms to reflect same-day availability for these electronic payments credits when reordering new stocks of forms.

Final Regulatory Flexibility Act Analysis

Two of the three requirements of a final regulatory flexibility analysis (5

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

One commenter stated that one of the revisions to the Commentary to § 229.19(a), which prohibits banks from considering checks received before 2:00 p.m. as the next day's deposits, would hurt small rural banks that close their teller windows before 2:00 p.m. to meet courier schedules. (See discussion in above preamble.) Under the Board's Commentary revision, certain remote banks may be unable to collect checks received for deposit close to the cut-off hour of 2:00 p.m., and consequently such checks may be returned later than checks deposited in time to meet the day's courier schedule. It is possible that the late return could increase the risk that the bank will have to make funds available before the check is returned. The Board believes that the risk associated with possible late returns applies only to a small number of remote banks and is dependent on the banks' location, courier schedule, and availability policy. The Board believes that the effect of the revision on small rural banks is minimal and that it would not be practical to attempt to define an exception to the cut-off hour provisions to address these situations.

List of Subjects in 12 CFR Part 229

Banks, banking; Federal Reserve System.

For the reasons set out in the preamble, Title 12, Chapter II, Part 229 of the Code of Federal Regulations is amended as follows:

PART 229—AVAILABILITY OF FUNDS AND COLLECTION OF CHECKS

1. The authority of Part 229 continues

to read as follows:

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

2. In § 229.2, paragraphs (e)(7), (z)(5), and (cc) are revised to read as follows:

§ 229.2 Definitions.

(e) "Bank" means—

(7) An "agency" or a "branch" of a "foreign bank" as defined in section 1(b) of the International Banking Act (12 U.S.C. 3101).

(z) "Paying bank" means—

(5) The state or unit of general local government on which a check is drawn and to which it is sent for payment or collection.

(cc) "Returning bank" means a bank (other than the paying or depositary bank) handling a returned check or notice in lieu of return. A returning bank is also a collecting bank for purposes of U.C.C. 4-202(2).

3. In § 229.13, the last sentence of paragraph (e)(2) concluding text is revised to read as follows:

§ 229.13 Exceptions.

(2) *Overdraft and returned check fees.* * * * The notice must state that the customer may be entitled to a refund of overdraft or returned check fees that are assessed if the check subject to the exception is paid and how to obtain a refund.

4. In § 229.16, the last sentence of paragraph (c)(3) concluding text is revised to read as follows:

§ 229.16 Specific availability policy disclosure.

(3) *Overdraft and returned check fees.* * * * The notice must state that the customer may be entitled to a refund of overdraft or returned check fees that are assessed if the check subject to the delay is paid and how to obtain a refund.

5. In § 229.19, paragraph (e) is revised to read as follows:

§ 229.19 Miscellaneous.

(e) *Holds on other funds.* (1) A

depository bank that receives a check for deposit in an account may not place a hold on any funds of the customer at the bank, where—

(i) The amount of funds that are held exceeds the amount of the check; or

(ii) The funds are not made available for withdrawal within the times specified in §§ 229.10, 229.11, 229.12, and 229.13.

(2) A depository bank that cashes a check for a customer over the counter, other than a check drawn on the depository bank, may not place a hold on funds in an account of the customer at the bank, if—

(i) The amount of funds that are held exceeds the amount of the check; or

(ii) The funds are not made available for withdrawal within the times specified in §§ 229.10, 229.11, 229.12, and 229.13.

6. In § 229.31, the last sentence of paragraph (b) concluding text is revised to read as follows:

§ 229.31 Returning bank's responsibility for return of checks.

(b) *Unidentifiable depository bank.* * * * A returning bank that receives a returned check from a paying bank under § 229.30(b), or from a returning bank under this paragraph, but that is able to identify the depository bank, must thereafter return the check expeditiously to the depository bank.

7. In § 229.32, the word "or" is removed at the end of paragraph (a)(2)(ii), paragraph (a)(2)(iii) is redesignated as paragraph (a)(2)(iv), and a new paragraph (a)(2)(iii) is added to read as follows:

§ 229.32 Depository bank's responsibility for returned checks.

(iii) If the address in the indorsement is not in the same check processing region as the address associated with the routing number of the bank in its indorsement or the check, at a location consistent with the address in the indorsement and at a branch or head office associated with the routing number in the bank's indorsement; or

8. In § 229.34, paragraph (a)(1), (a) concluding text, paragraph (b) introductory text, (b)(1), and (b) concluding text are revised to read as follows:

§ 229.34 Warranties by paying and returning bank.

(a) *Warranties.* * * *

(1) The paying bank, or in the case of a check payable by a bank and payable through another bank, the bank by which the check is payable, returned the check within its deadline under the U.C.C., Regulation J (12 CFR Part 210), or § 229.30(c) of this part;

These warranties are not made with respect to checks drawn on the Treasury of the United States, U.S. Postal Service money orders, or checks drawn on a state or a unit of general local government that are not payable through or at a bank.

(b) *Warranty of notice of nonpayment.* Each paying bank that gives a notice of nonpayment warrants to the transferee bank, to any subsequent transferee bank, to the depository bank, and to the owner of the check that—

(1) The paying bank, or in the case of a check payable by a bank and payable through another bank, the bank by which the check is payable, returned or will return the check within its deadline under the U.C.C., Regulation J (12 CFR Part 210), or § 229.30(c) of this part;

These warranties are not made with respect to checks drawn on a state or a unit of general local government that are not payable through or at a bank.

9. In § 229.30(d), the first sentence is revised to read as follows:

§ 229.38 Liability.

(d) *Responsibility for back of check.* A paying bank, or in the case of a check payable through the paying bank and payable by another bank, the bank by which the check is payable, is responsible for damages under paragraph (a) of this section to the extent that the condition of the check when issued by it or its customer adversely affects the ability of a bank to indorse the check legibly in accordance with § 229.35.

Appendix A—[Amended]

10. Appendix A is amended by adding a new routing number to the list, under the heading *Federal Home Loan Banks*, in numerical order, as follows:

1130 1750 8

Appendix E—[Amended]

Section 229.2—[Amended]

11. The Commentary to § 229.2 is amended as follows:

a. In paragraph (d), removing the last sentence of the second paragraph and replacing it with two new sentences.

(d) *Available for withdrawal.* * * * For purposes of this regulation, funds are considered available for withdrawal even though they are being held by the bank to satisfy an obligation of the customer other than the customer's potential liability for the return of the check. For example, funds are available for withdrawal even though they are being held by a bank to satisfy a garnishment, tax levy, or court order restricting disbursements from the account, or to satisfy the customer's liability arising from the certification of a check, sale of a cashier's or teller's check, guaranty or acceptance of a check, or similar transaction.

b. In paragraph (e), revising the second paragraph.

(e) *Bank.* * * * "Bank" is defined to include depository institutions, such as commercial banks, savings banks, savings and loan associations, and credit unions as defined in the Act, and U.S. branches and agencies of foreign banks. For purposes of Subpart B, the term does not include corporations organized under section 25(a) of the Federal Reserve Act, 12 U.S.C. 611-631 (Edge corporations) or corporations having an agreement or undertaking with the Board under section 25 of the Federal Reserve Act, 12 U.S.C. 601-604a (agreement corporations). For purposes of subpart C, and in connection therewith, Subpart A, any Federal Reserve Bank, Federal Home Loan Bank, or any other person engaged in the business of banking is regarded as a bank. The phrase "any other person engaged in the business of banking" is derived from U.C.C. 1-201(4), and is intended to cover entities that handle checks for collection and payment, such as Edge and agreement corporations, commercial lending companies under 12 U.S.C. 3101, certain industrial banks, and private bankers, so that virtually all checks will be covered by the same rules for forward collection and return, even though they may not be covered by the requirements of Subpart B. For the purposes of Subpart C, and in connection therewith, Subpart A, the term may also include a state or a unit of general local government to the extent that it pays warrants or other drafts drawn directly on the state or local government itself, and the warrants or other drafts are sent to the state or local government for payment or collection.

c. In paragraphs (f) and (g), revising the last paragraph.

(f) *Banking day* and (g) *Business day.* * * * The definition of "banking day" is phrased in terms of when "an office of a bank is open" to indicate that a bank may observe a banking day on a per-branch basis. A deposit

made at an ATM or off-premise facility (such as a remote depository or a lock box) is considered made at the branch holding the account into which the deposit is made for the purpose of determining the day of deposit. All other deposits are considered made at the branch at which the deposit is received. For example, under § 229.19(a)(1), funds deposited at an ATM are considered deposited at the time they are received at the ATM. The day of deposit for such funds is determined by the banking day at the account-holding branch at the time the funds are received at the ATM. Similarly, under § 229.19(a)(3), funds deposited to a night depository, lock box, or similar facility are considered deposited when the funds are removed from the facility and are available for processing. If such a facility is not on the premises of a branch, the day of deposit is determined by the banking day at the account-holding branch. If such a facility is on branch premises, the day of deposit is determined by the banking day at the branch at which the deposit is received, whether or not it is the account-holding branch.

d. In paragraph (i), removing the second sentence and replacing it with two new sentences, and removing the last sentence and replacing it with four new sentences.

(i) *Cashier's check.* * * * The definition of cashier's check includes checks provided to a customer of the bank in connection with customer deposit account activity, such as account disbursements and interest payments. The definition also includes checks acquired from a bank by noncustomers for remittance purposes, including loan disbursement checks.

* * * The definition excludes checks that a bank draws on itself for other purposes, such as to pay employees and vendors, and checks issued by the bank in connection with a payment service, such as a payroll or a bill-paying service. Cashier's checks are generally sold by banks to substitute the bank's credit for the customer's credit and thereby enhance the collectibility of the checks. A check issued in connection with a payment service is generally provided as a convenience to the customer rather than as a guarantee of the check's collectibility. In addition, such checks are often more difficult to distinguish from other types of checks than are cashier's checks as defined by this regulation.

e. In paragraph (k), revising the last paragraph.

(k) *Check.* * * * The definition of check does not include an instrument payable in a foreign currency (i.e., other than in United States money as defined in 31 U.S.C. 5101) or a credit card draft (i.e., a sales draft used by a merchant or a draft generated by a bank as a result of a cash advance). The definition of check includes a check that a bank may supply to a customer as a means of accessing a credit line without the use of a credit card.

f. In paragraph (u), adding a new

sentence to the end of the second paragraph.

(u) *Noncash item.* * * *
* * * (In the context of this definition, "paying bank" refers to the paying bank as defined for purposes of Subpart C.)

g. In paragraph (cc), revising the last sentence and adding a new sentence immediately following.

(cc) *Returning bank.* * * * A returning bank is also a collecting bank for the purpose of a collecting bank's duty to act seasonably under U.C.C. 4-202(2) and is analogous to a collecting bank for purposes of final settlement. (See Commentary to § 229.35(b).)

h. In paragraph (gg), removing the fourth sentence and replacing it with seven new sentences.

(gg) *Teller's check* * * * The definition does not include checks that are drawn by a nonbank on a nonbank even if payable through or at a bank. The definition includes checks provided to a customer of the bank in connection with customer deposit account activity, such as account disbursements and interest payments. The definition also includes checks acquired from a bank by a noncustomer for remittance purposes, including loan disbursement checks. The definition excludes checks used by the bank to pay employees or vendors and checks issued by the bank in connection with a payment service, such as a payroll or a bill-paying service. Teller's checks are generally sold by banks to substitute the bank's credit for the customer's credit and thereby enhance the collectibility of the checks. A check issued in connection with a payment service is generally provided as a convenience to the customer rather than as a guarantee of the check's collectibility. In addition, such checks are often more difficult to distinguish from other types of checks than are teller's checks as defined by this regulation. * * *

i. Adding a new paragraph (kk) immediately following paragraph (ii).

(kk) *Unit of general local government* is defined to include a city, county, parish, town, township, village, or other general purpose political subdivision of a state. The term does not include special purpose units, such as school districts, water districts, or Indian nations.

Section 229.10—[Amended]

12. The Commentary to § 229.10(c) is amended as follows:

a. In paragraph (c) introductory text, revising the last sentence and adding two sentences to follow.

(c) *Certain check deposits.* * * * For the purposes of this section, all checks drawn on a Federal Reserve Bank or a Federal Home Loan Bank that contain in the MICR line a routing number that is listed in Appendix A are subject to the next-day availability requirement if they are deposited in an account held by a payee of the check and in person to an employee of the depository

bank, regardless of the purposes for which the checks were issued. For all new accounts, even if the new account exception is not invoked, traveler's checks must be included in the \$5,000 aggregation of checks deposited on any one banking day that are subject to the next-day availability requirement. (See § 229.13(a).)

b. Revising the heading "Deposit at Staffed Teller Station" and the first paragraph under that heading.

Deposits Made to an Employee of the Depository Bank

In most cases, next-day availability of the proceeds of checks subject to this section is conditioned on the deposit of these checks in person to an employee of the depository bank. If the deposit is not made to an employee of the depository bank on the premises of such bank, the proceeds of the deposit must be made available for withdrawal by the start of business on the second business day after deposit, under paragraph (c)(2) of this section. For example, second-day availability rather than next-day availability would be allowed for deposits of checks subject to this section made at a proprietary ATM (and at a nonproprietary ATM under the permanent schedule), night depository, through the mail or a lock box, or at a teller station staffed by a person that is not an employee of the depository bank. Second-day availability may also be allowed for deposits picked up by an employee of the depository bank at the customer's premises; such deposits would be considered made upon receipt at the branch or other location of the depository bank.

c. Removing the heading "Fees for Withdrawals" and the paragraph appearing under it.

d. In the fifth paragraph under the heading "Special Deposit Slips," revising the second sentence.

Special Deposit Slips

* * * If a bank only provides the special deposit slips upon the request of a depositor, however, the teller must advise the depositor of the availability of the special deposit slips, or the bank must post a notice advising customers that the slips are available upon request. * * *

13. The Commentary to § 229.11(c) is amended by revising the first sentence to read as follows:

Section 229.11—Temporary Availability Schedule

(c) *Nonlocal checks.* Under the temporary schedule, funds deposited by nonlocal checks must be made available for withdrawal not later than the seventh business day following the banking day the funds are deposited, except in the case of deposits in accounts of banks located outside the 48 contiguous states. * * *

14. The Commentary to § 229.13(b) is amended by adding a new sentence after the second sentence in the first paragraph of paragraph (b) to read as follows:

Section 229.13—Exceptions

(b) *Large Deposits.* * * * When the large deposit exception is applied to deposits composed of both local and nonlocal checks, the depository bank has the discretion to choose the portion of the deposit to which it applies the exception. * * *

15. The Commentary to § 229.16 is amended by adding two new paragraphs to paragraph (a) and adding a new paragraph at the end of paragraph (b) to read as follows:

Section 229.16—Specific Availability Policy Disclosure

(a) *General.* * * *
The disclosure must reflect the policy and practice of the bank regarding availability as to most accounts and most deposits into those accounts. In disclosing the availability policy that it follows in most cases, a bank may provide a single disclosure that reflects one policy to all its transaction account customers, even though some of its customers may receive faster availability than that reflected in the policy disclosure. Thus, a bank need not disclose to some customers that they receive faster availability than that indicated in the disclosure. If, however, a bank has a policy of imposing delays in availability on any customers longer than those specified in its disclosure, those customers must receive disclosures that reflect the longer applicable availability periods.

A bank may disclose that funds are "available for withdrawal" on a given day notwithstanding the fact that the bank uses the funds to pay checks received before that day. For example, a bank may disclose that its policy is to make funds available from deposits of local checks on the second business day following the day of deposit, even though it may use the deposited funds to pay checks prior to the second business day; the funds used to pay checks in this example are not available for withdrawal until the second business day after deposit because the funds are not available for all uses until the second business day. (See the definition of "available for withdrawal" in § 229.2(d).)

(b) *Content of Specific Policy Disclosure.* * * *

A bank that provides availability based on when the bank generally receives credit for deposited checks need not disclose the time when a check drawn on a specific bank will be available for withdrawal. Instead, the bank may disclose the categories of deposits that must be available on the first business day after the day of deposit (deposits subject to § 229.10) and state the other categories of deposits and the time periods that will be applicable to those deposits. For example, a

bank might disclose the four-digit Federal Reserve routing symbol for local checks and indicate that such checks as well as certain nonlocal checks will be available for withdrawal on the first or second business day following the day of deposit, depending on the location of the particular bank on which the check is drawn, and disclose that funds from all other checks will be available on the second or third business day. The bank must also disclose that the customer may request a copy of the bank's detailed schedule that would enable the customer to determine the availability of any check and must provide such schedule upon request. A change in the bank's detailed schedule would not trigger the change in policy disclosure requirement of § 229.18(e).

Section 229.19—[Amended]

16. The Commentary to § 229.19 is amended as follows:

a. Adding a new sentence after the third sentence of the first paragraph of paragraph (a) and removing the last sentence of the last paragraph and adding a new paragraph at the end thereof:

(a) *When Funds Are Considered Deposited.* * * * Funds deposited to a deposit box in a bank lobby that is accessible to customers only during regular business hours are generally considered deposited when placed in the lobby box; a bank may, however, treat deposits to lobby boxes the same as deposits to night depositories (as provided in § 229.19(a)(3)), provided a notice appears on the lobby box informing the customer when such deposits will be considered received. * * *

A bank is not required to remain open until 2:00 p.m. If a bank closes before 2:00 p.m., deposits received after the closing may be considered received on the next banking day. Further, as § 229.2(f) defines the term "banking day" as the portion of a business day on which a bank is open to the public for substantially all of its banking functions, a day, or a portion of a day, is not necessarily a banking day merely because the bank is open for only limited functions, such as keeping drive-in or walk-up teller windows open, when the rest of the bank is closed to the public. For example, a banking office that usually provides a full range of banking services may close at 12:00 noon but leave a drive-in teller window open for the limited purpose of receiving deposits and making cash withdrawals. Under those circumstances, the bank is considered closed and may consider deposits received after 12:00 noon as having been received on the next banking day. The fact that a bank may reopen for substantially all of its banking functions after 2:00 p.m., or that it continues its back office operations throughout the day, would not affect this result. A bank may not, however, close individual teller stations and reopen them for next-day's business before 2:00 p.m. during a banking day.

b. In paragraph (e), revising the second paragraph and adding a third paragraph.

(e) *Holds on other funds.* * * * This paragraph clarifies that if a customer deposits a check in an account (as defined in § 229.2(a)), the bank may not place a hold on any of the customer's funds so that the funds that are held exceed the amount of the check deposited or the total amount of funds held are not made available for withdrawal within the times required in this subpart. For example, if a bank places a hold on funds in a customer's nontransaction account, rather than a transaction account, for deposits made to the customer's transaction account, the bank may place such a hold only to the extent that the funds held do not exceed the amount of the deposit and the length of the hold does not exceed the time periods permitted by this regulation.

These restrictions also apply to holds placed on funds in a customer's account (as defined in § 229.2(a)) if a customer cashes a check at a bank (other than a check drawn on that bank) over the counter. The regulation does not prohibit holds that may be placed on other funds of the customer for checks cashed over the counter, to the extent that the transaction does not involve a deposit to an account. A bank may not, however, place a hold on any account when an on us check is cashed over the counter. On us checks are considered finally paid when cashed (see U.C.C. 4-213(1)(a)).

17. The Commentary to § 229.20(c) is revised to read as follows:

Section 229.20 Relation to State Law

(c) *Standards for preemption.* This section describes the standards the Board will use in making determinations on whether federal law will preempt state laws governing funds availability. A provision of state law is considered inconsistent with federal law if it permits a depository bank to make funds available to a customer in a longer period of time than the maximum period permitted by the Act and this regulation. For example, a state law that permits a hold of four business days or longer for local checks permits a hold that is longer than that permitted under the Act and this regulation, and therefore is inconsistent and preempted. State availability schedules that provide for availability in a shorter period of time than required under Regulation CC supersede the federal schedule.

Under a state law, some categories of deposits could be available for withdrawal sooner or later than the time required by this subpart, depending on the composition of the deposit. For example, the Act and this regulation (§ 229.10(c)(1)(vii)) require next-day availability for the first \$100 of the aggregate deposit of local or nonlocal checks on any day, and a state law could require next-day availability for any check of \$100 or less that is deposited. Under the Act and this regulation, if either one \$150 check or three \$50 checks are deposited on a given day, \$100 must be made available for withdrawal on the next business day, and \$50 must be made available in accordance with the local or

nonlocal schedule. Under the state law, however, the two deposits would be subject to different availability rules. In the first case, none of the proceeds of the deposit would be subject to next-day availability; in the second case, the entire proceeds of the deposit would be subject to next-day availability. In this example, because the state law would, in some situations, permit a hold longer than the maximum permitted by the Act, this provision of state law is inconsistent and preempted in its entirety.

In addition to the differences between state and federal availability schedules, a number of state laws contain exceptions to the state availability schedules that are different from those provided under the Act and this regulation. The state exceptions continue to apply only in those cases where the state schedule is shorter than or equal to the federal schedule, and then only up to the limit permitted by the Regulation CC schedule. Where a deposit is subject to a state exception under a state schedule that is not preempted by Regulation CC and is also subject to a federal exception, the hold on the deposit cannot exceed the hold permissible under the federal exception in accordance with Regulation CC. In such cases, only one exception notice is required, in accordance with § 229.13(g). This notice need only include the applicable federal exception as the reason the exception was invoked. For those categories of checks for which the state schedule is preempted by the federal schedule, only the federal exceptions may be used.

State laws that provide maximum availability periods for categories of deposits that are not covered by the Act would not be preempted. Thus, state funds availability laws that apply to funds in time and savings deposits are not affected by the Act or this regulation. In addition, the availability schedules of several states apply to "items" deposited to an account. The term "items" may encompass deposits, such as nonnegotiable instruments, that are not subject to the Regulation CC availability schedules. Deposits that are not covered by Regulation CC continue to be subject to the state availability schedules. State laws that provide maximum availability periods for categories of institutions that are not covered by the Act would also not be preempted. For example, a state law that governs money market mutual funds would not be affected by the Act or this regulation.

Generally, state rules governing the disclosure or notice of availability policies applicable to accounts are also preempted, if they are different from the federal rules. Nevertheless, a state law requiring disclosure of funds availability policies that apply to deposits other than "accounts," such as savings or time deposits, are not inconsistent with the Act and this subpart. Banks in these states would have to follow the state disclosure rules for these deposits.

Section 229.30—[Amended]

18. The Commentary to § 229.30 is amended as follows:

a. In paragraph (a), under the fourth numbered example, adding a new

sentence to the end of the third paragraph and adding a new sentence to the end of the eighth paragraph.

(a) *Return of checks.* * * *

Examples

* * * * *
4. * * *

* * * If a paying bank returns a check on its banking day of receipt without paying for the check, as permitted under U.C.C. 4-302(a), and receives settlement for the returned check from a returning bank, it must promptly pay the amount of the check to the collecting bank from which it received the check.

* * * Also, a paying bank is not responsible for failure to make expeditious return to a party that has breached a presentment warranty under U.C.C. 4-207(1), notwithstanding that the paying bank has returned the check. (See Commentary to § 229.30(a).)

b. In paragraph (b), revising the fourth sentence of the second paragraph and adding two new sentences to immediately follow, and revising the first sentence of the third paragraph.

(b) *Unidentifiable depositary bank.* * * *
* * * A paying bank returning a check under this paragraph to a bank that has not agreed to handle the check expeditiously must advise that bank that it is unable to identify the depositary bank. This advice must be conspicuous, such as a stamp on each check for which the depositary bank is unknown if such checks are commingled with other returned checks, or, if such checks are sent in a separate cash letter, by one notice on the cash letter. The returned check may not be prepared for automated return. * * *

The sending of a check to a bank that handled the check for forward collection under this paragraph is not subject to the requirements for expeditious return by the paying bank. * * *

c. Revising the first paragraph of paragraph (f).

(f) *Notice in Lieu of Return.* A check that is lost or otherwise unavailable for return may be returned by sending a legible copy of both sides of the check or, if such a copy is not available to the paying bank, a written notice of nonpayment containing the information specified in § 229.33(b). The copy or written notice must clearly indicate it is a notice in lieu of return and must be handled in the same manner as other returned checks. Notice by telephone, telegraph, or other electronic transmission, other than a legible facsimile or similar image transmission of both sides of the check, does not satisfy the requirements for a notice in lieu of return. The requirement for a writing and the indication that the notice is a substitute for the returned check is necessary so that the returning and depositary banks are informed that the notice carries value. Notice in lieu of return is permitted only when a bank does not have and cannot obtain possession of the

check or must retain possession of the check for protest. A check is not unavailable for return if it is merely difficult to retrieve from a filing system or from storage by a keeper of checks in a truncation system. A notice in lieu of return may be used by a bank handling a returned check that has been lost or destroyed, including when the original returned check has been charged back as lost or destroyed as provided in § 229.35(b). A bank using a notice in lieu of return gives a warranty under § 229.34(a)(4) that the original check has not been and will not be returned.

Section 229.31—[Amended]

19. The Commentary to § 229.31 is amended as follows:

a. In paragraph (b), revising the last sentence of the first paragraph and revising the last paragraph.

(b) *Unidentifiable depositary bank.* * * * In the limited cases where the returning bank cannot identify the depositary bank, the returning bank may send the returned check to a returning bank that agrees to handle the returned check for expeditious return under § 229.31(a), or it may send the returned check to a bank that handled the check for forward collection, even if that bank does not agree to handle the returned check expeditiously under § 229.31(a).

As in the case of a paying bank returning a check under § 229.30(b), a returning bank returning a check under this paragraph to a bank that has not agreed to handle the check expeditiously must advise that bank that it is unable to identify the depositary bank. This advice must be conspicuous, such as a stamp on each check for which the depositary bank is unknown if such checks are commingled with other returned checks, or, if such checks are sent in a separate cash letter, by one notice on the cash letter. The returned check may not be prepared for automated return.

b. In paragraph (c), revising the parenthetical at the end of the second paragraph.

(c) *Settlement.* * * *
* * * (See § 229.36(d) and Commentary to § 229.35(b).)

c. In paragraph (f), adding a new sentence before the parenthetical phrase.

(f) *Notice in lieu of return.* * * * Notice in lieu of return is permitted only when a bank does not have and cannot obtain possession of the check or must retain possession of the check for protest. A check is not unavailable for return if it is merely difficult to retrieve from a filing system or from storage by a keeper of checks in a truncation system. * * *

20. The Commentary to § 229.32(a) is amended by redesignating item 2(iii) as 2(iv), adding a new item 2(iii), and adding a new paragraph after the last paragraph to read as follows:

Section 229.32—Depositary Bank's Responsibility for Returned Checks

(a) *Acceptance of returned checks.* * * *
2. * * *

(iii) The depositary bank must accept returned checks at the address in its indorsement and at an address associated with its routing number in the indorsement if the written address in the indorsement and the address associated with the routing number in the indorsement are not in the same check processing region. Under §§ 229.30(g) and 229.31(g), a paying or returning bank may rely on the depositary bank's routing number in its indorsement in handling returned checks and is not required to send returned checks to an address in the depositary bank's indorsement that is not in the same check processing region as the address associated with the routing number in the indorsement.

Under § 229.33(d), a depositary bank receiving a returned check or notice of nonpayment must send notice to its customer by its midnight deadline or within a longer reasonable time.

Section 229.33—[Amended]

21. The Commentary to § 229.33 is amended as follows:

a. In paragraph (a), adding a new paragraph at the end thereof.

(a) *Requirement.* * * *

Unless the returned check is used to satisfy the notice requirement, the requirement for notice is independent of and does not affect the requirements for timely and expeditious return of the check under § 229.30 and the U.C.C. (See § 229.30(a).) If a paying bank fails both to comply with this section and to comply with the requirements for timely and expeditious return under § 229.30 and the U.C.C. and Regulation J (12 CFR Part 210), the paying bank shall be liable under either this section or such other requirements, but not both. (See § 229.38(b).) A paying bank is not responsible for failure to give notice of nonpayment to a party that has breached a presentment warranty under U.C.C. 4-207(1), notwithstanding that the paying bank may have returned the check.

(See U.C.C. 4-207(1) and 4-302.)

b. In paragraph (d), revising the first sentence.

(d) *Notification to Customer.* This paragraph requires a depositary bank to notify its customer of nonpayment upon receipt of a returned check or notice of nonpayment, regardless of the amount of the check or notice. * * *

22. The Commentary to § 229.34(a) is amended by revising the first and last sentence thereof to read as follows:

Section 229.34—Warranties by Paying Bank and Returning Bank

(a) *Warranty of returned checks.* This paragraph includes warranties that a returned check, including a notice in lieu of return, was returned by the paying bank, or in the case of a check payable by a bank and

payable through another bank, the bank by which the check is payable, within the deadline under the U.C.C., Regulation J, or § 229.30(c); that the paying or returning bank is authorized to return the check; that the returned check has not been materially altered; and that, in the case of notice in lieu of return, the original check has not and will not be returned (see Commentary to § 229.30(f)). * * * These warranties do not apply to checks drawn on the United States Treasury, to Postal Service money orders, or to checks drawn on a state or a unit of general local government that are not payable through or at a bank (see § 229.42).

Section 229.35—[Amended]

23. The Commentary to § 229.35 is amended as follows:

a. In paragraph (a), adding two sentences to the end of the fourth paragraph, revising the first two sentences in the fifth paragraph, and adding a sentence to the end of the last paragraph.

(a) *Indorsement Standards.* * * *

* * * Depository banks should not include information that can be confused with required information. For example, a nine-digit zip code could be confused with the nine-digit routing number.

A depository bank is not required to place a street address in its indorsement; however, a bank may want to put an address in its indorsement in order to limit the number of locations at which it must accept returned checks. In instances where this address is not consistent with the routing number in the indorsement, the depository bank is required to accept returned checks at a branch or head office consistent with the routing number. Banks should note, however, that § 229.32 requires a depository bank to accept returned checks at the location(s) it accepts forward collection checks. * * *

* * * The standard requires collecting and returning banks to indorse the check for tracing purposes.

b. In paragraph (b), adding four sentences to the end of the fifth paragraph and adding a new paragraph after the fifth paragraph.

(b) *Liability of bank handling check.* * * *

* * * Nor does this paragraph affect a collecting bank's accountability under U.C.C. 4-211 (2) and (3) and 4-213(3). A collecting bank becomes accountable upon receipt of final settlement as provided in the foregoing U.C.C. sections. The term "final settlement" in §§ 229.31(c), 229.32(b), and 229.36(d) is intended to be consistent with the use of the term "final settlement" in the U.C.C. (e.g., U.C.C. 4-211, 4-212, and 4-213). (See also § 229.2(cc) and Commentary.)

This paragraph also provides that a bank may have the rights of a "holder" based on the handling of the check for collection or return. A bank may become a holder or a holder in due course regardless of whether prior banks have complied with the indorsement standard in § 229.35(a) and Appendix D.

24. The Commentary to § 229.37 is amended by revising the second sentence of the first paragraph and revising the second paragraph to read as follows:

Section 229.37 Variations by Agreement

* * * To achieve consistency, the official comment to U.C.C. 4-103(1) (which in turn follows U.C.C. 1-201(3)) should be followed in construing this section. * * *

The Board has not followed U.C.C. 4-103(2), which permits Federal Reserve regulations and operating letters, clearinghouse rules, and the like to apply to parties that have not specifically assented. Nevertheless, this section does not affect the status of such agreements under the Uniform Commercial Code.

25. In the Commentary to § 229.38(d), the first two sentences of the second

paragraph are revised to read as follows:

Section 229.38 Liability

(d) *Responsibility for back of check.* * * *

The paying bank or, in the case of a check payable through the paying bank and payable by another bank, the bank by which the check is payable, is responsible for the condition of the check when it is issued by it or its customer. (It would not be responsible for a check issued by a person other than such a bank or customer.) * * *

Appendix C—[Amended]

26. In the Commentary to Appendix C, under the heading "Models C-1 Through C-7 Generally," a new paragraph is added after the fifth paragraph to read as follows:

Models C-1 Through C-7 Generally

Banks that have used model forms C-1, C-2, or C-3 or have used forms C-4, C-5, C-6, or C-7 (which give social security benefits and payroll payments as examples of preauthorized credits available the day after deposit) and that at the same time follow Treasury regulations (31 CFR Part 210) and ACH association rules requiring that these credits be made available on the day the bank receives the funds are protected from civil liability under § 229.21(e). Such banks are encouraged to disclose same-day availability for those electronic payments when reordering supplies of forms.

By order of the Board of Governors of the Federal Reserve System, March 31, 1989.

William W. Wiles,

Secretary of the Board.

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