

RESCINDED

Consumer Affairs Laws and
Regulations Section 1336

This document and any attachments are superseded by Comptroller's Handbook - Consumer Compliance - Depository Services.

Check 21

The Expedited Funds Availability Act (EFA) was enacted in August 1987 and became effective in September 1988. Regulation CC (12 CFR Part 229), issued by the Board of Governors of the Federal Reserve System, implements the EFA. Regulation CC was amended to include Subpart D, implementing the Check Clearing for the 21st Century Act (Check 21), in October 2003. This Handbook Section provides information on Subpart D, the Check 21 section of the regulation. For a discussion of Parts A-C of the regulation, refer to the [Expedited Funds Availability Act Handbook Section](#).

Check 21 authorizes the use of a new negotiable instrument called a “substitute check” to facilitate the broader use of electronic check processing and sets forth requirements that affect savings associations that create or receive substitute checks, including consumer disclosures and expedited recredit procedures. Check 21 does not require a savings association to use electronic check processing, receive

electronic presentment or create a substitute check. However, certain provisions of the Check 21 Act will affect all savings associations, even those that do not choose to create substitute checks.

SUBPART D – SUBSTITUTE CHECKS

Whether a savings association will or will not function as a “reconverting bank”,¹ the interlinked nature of the payments system virtually guarantees that every savings association will at some time receive a substitute check that is subject to the provisions of Subpart D, the Check 21 section of Regulation CC. While some associations will rapidly migrate toward electronic check exchange, others will proceed more hesitantly. Regardless, because the Check 21 Act provides that a properly prepared substitute check is the “legal equivalent of the original check for all purposes,” all savings associations must be prepared to *accept* a substitute check in place of the original after the Act’s effective date of October 28, 2004.

One of a savings association’s regulatory compliance obligations is to apprise customers of their rights under the new law through a consumer awareness disclosure. The association must provide the disclosure if the customer receives either of the following:

¹ A reconverting bank is the bank that creates a substitute check; if a nonbank creates a substitute check, the reconverting bank is the first bank to transfer, present, or return the substitute check (or the first paper or electronic representation of that substitute check) for consideration.

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- Cancelled checks with their periodic account statements.
- Substitute checks on an occasional basis.

A savings association that provides a substitute check to a customer also must be prepared to comply with the Check 21 Act's expedited recredit procedure for addressing errors relating to substitute checks. Even if the customer does not receive actual cancelled checks in a monthly statement but instead receives a truncated summary, the individual may eventually receive a substitute check. Receipt of a substitute check may be in response to a request for a check or a copy of a check or because a check that the customer deposited was returned unpaid to the customer in the form of a substitute check. Some increase in the potential for duplicate posting (substitute check and original) may also involve a degree of consumer education and explanation. The regulation specifies the appropriate timing for the distribution of the consumer awareness disclosure and also provides model language. Finally, savings associations will likely want to train their personnel so that they can adequately convey to customers the impact of this new instrument in the payments system.

General Provisions Governing Substitute Checks – § 229.51

A substitute check for which a savings association has provided the warranties described in 12 CFR § 229.52² is the legal equivalent of an original check if the substitute check:

- Accurately represents all of the information on the front and back of the original check.
- Bears the legend “This is a legal copy of your check. You can use it the same way you would use the original check.”³

The reconverting bank must adhere to Regulation CC's standards for preserving bank indorsements and identifications. A reconverting bank that receives consideration for a substitute check that it transfers, presents, or returns also is the first bank to provide the warranties and the indemnity described below.

Substitute Check Warranties and Indemnity – §§ 229.52 and 229.53

Starting with the reconverting bank, any savings association that transfers, presents, or returns a substitute check (or a paper or electronic representation of a substitute check) and receives consideration for that check warrants that the substitute check meets the legal equivalence requirements and that a check that has already been paid will not be presented for subsequent payment (§ 229.52).

² A person other than a bank that creates a substitute check could transfer that check only by agreement unless and until a bank provides the substitute check warranties.

³ A savings association may not vary the language of the legal equivalence legend.

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Such a savings association also provides an indemnity to cover losses that the recipient and any subsequent recipient of the substitute check incurs due to the receipt of a substitute check instead of the original check (§229.53).

Expedited Recredit for Consumers – § 229.54

Section 229.54(a) sets forth the conditions under which a consumer may make an expedited recredit claim for losses associated with the consumer's receipt of a substitute check. To use the expedited recredit procedure, the consumer must be able to assert in good faith that:

- The association charged the consumer's account for a substitute check that was provided to the consumer.
- The association improperly charged the consumer's account or the consumer has a warranty claim.
- The consumer suffered a loss.
- The consumer needs the original check or a sufficient copy to determine the validity of the claim.

Section 229.54(a) sets forth the conditions under which a consumer may make an expedited recredit claim for losses associated with the consumer's receipt of a substitute check.

To make a claim, the consumer must comply with the timing, content, and form requirements in § 229.54(b). This section generally provides that the savings association that holds the consumer's account must receive a consumer's claim no later than the fortieth calendar day after the later of:

- The calendar day on which the association mailed (or delivered by a means agreed to by the consumer) the periodic statement describing the contested transaction; or
- The calendar day on which the association mailed (or delivered by a means agreed to by the consumer) the substitute check itself.

Section 229.54(b)(1)(ii) requires the savings association to give the consumer an additional, reasonable period of time if the consumer experiences "extenuating circumstances" that prevent timely submission of the claim.

The commentary to § 229.60 provides that the savings association may voluntarily give the consumer more time to submit a claim than the rule allows.

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Under § 229.54(b)(2)(ii), a complaint is not considered complete, and thus does not constitute a claim, until it contains all of the required information the rule requires. The rule requires the claim to contain all of the following information:⁴

- A description of why the consumer believes the account was improperly charged or the nature of the consumer's warranty claim.
- A statement that the consumer has suffered a loss and an estimate of the amount of the loss.
- A reason why the original check (or a copy of the check that is better than the substitute check the consumer already received) is necessary to determine whether the consumer's claim is valid.
- Sufficient information to allow the association to identify the substitute check and investigate the claim.

A savings association, in its discretion, may require the consumer to submit the claim in writing. If a consumer makes an oral claim to a savings association that requires a written claim, the association must inform the consumer of the in-writing requirement at that time. Under those circumstances, the savings association must receive the written claim by the later of ten business days from the date of an oral claim or the expiration of the consumer's initial 40-day period for submitting a timely claim. As long as the original oral claim fell within the 40-day requirement for notification and the savings association received a complete written claim within the additional ten-day window, the claim meets the timing requirements (§§ 229.54(b)(1) and 229.54(b)(3)), even if the savings association received the written claim after the expiration of the initial 40-day period.

The Savings Association's Action on Claims

Section 229.54(c) requires a savings association to act on the consumer's claim no later than the tenth business day after the banking day on which it received the consumer's claim:

- If the savings association determines that the consumer's claim is valid, it must recredit the consumer's account no later than the end of the business day after the banking day on which it makes that determination. The amount of the recredit should be for the amount of the consumer's loss, up to the amount of the substitute check, plus interest on that amount if the account is an interest-bearing account. The association must then notify the consumer of the recredit using the notice discussed in the next section (*Notices Relating to Expedited Recredit Claims*).

⁴ If a consumer submits an incomplete complaint, the savings association must so inform the consumer and must tell the consumer what information is missing.

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- If the association determines that the consumer's claim is invalid, it must notify the consumer of that decision using the notice discussed in the next section (*Notices Relating to Expedited Recredit Claims*).
- If the association has not determined the validity of the consumer's claim by the tenth business day after the banking day on which the savings association received the claim, the savings association must recredit the consumer's account for the amount of the consumer's loss, up to the amount of the substitute check or \$2,500, whichever is less. The association also must recredit interest on that amount if the consumer's account is an interest-bearing account. The savings association must send a notice to that effect to the consumer using the notice discussed in the next section (*Notices Relating to Expedited Recredit Claims*). If the consumer's loss was more than \$2,500, the savings association has until the end of the 45th calendar day from the date of the claim to recredit any remaining amount of the consumer's loss, up to the amount of the substitute check (plus interest), unless it determines prior to that time that the claim was invalid and notifies the consumer of that decision.

Section 229.54(d) generally requires that recredited funds receive next day availability. However, a savings association that provisionally recredits funds pending further investigation may invoke safeguard exceptions to delay availability of the recredit under the limited circumstances described in § 229.54(d)(2). The safeguard exceptions apply to new accounts and repeatedly overdrawn accounts, or if the savings association has reasonable cause to suspect the claim is fraudulent. A savings association may delay availability of a provisionally recredited amount until the start of the earlier of:

- The business day after the banking day on which the association determines the consumer's claim is valid, or
- The 45th calendar day after the banking day on which the association received the claim if the account is new, the account is overdrawn, or the savings association has reasonable cause to believe that the claim is fraudulent. When the savings association delays availability under this section, it may not impose overdraft fees on checks drawn against the provisionally credited funds until the fifth calendar day after the day on which the savings association sent the notice regarding the delayed availability.

If, after providing the recredit, the savings association determines that the consumer's claim was invalid, the savings association may reverse the recredit. This reversal must be accompanied by a consumer notification using the notice discussed below (*Notices Relating to Expedited Recredit Claims*).

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Notices Relating to Expedited Recredit Claims

Section 229.54(e) outlines the requirements for providing consumer notices related to expedited recredit:

- The savings association must send the notice of recredit no later than the business day after the banking day on which the association recredits the consumer's account. This notice must include the amount of the recredit and the date the recredited funds will be available for withdrawal.
- The savings association must send notice that the consumer's claim is not valid no later than the business day after the banking day on which the association makes this determination. This notice must include the original check or a sufficient copy of it (except as provided in § 229.58, see below). The notice must demonstrate to the consumer why the claim is not valid. The notice also must include either any information or documentation that the savings association used in making its determination or an indication that the consumer may request copies of this information.
- The savings association must send the notice of a reversal of recredit no later than the business day after the banking day on which the savings association made the reversal. The notice must include all of the information required in a notice of invalid claim plus the amount (including interest) and date of the reversal § 229.54(e)(3)(i).

Appendix C to Regulation CC contains model forms (models C-23 through C-25) that a savings association may use to craft the various notices required under § 229.54(e). Although there is no statutory safe harbor for appropriate use of these models, the Board published them to assist banks in complying with § 229.54(e).

Expedited Recredit for Savings Associations – § 229.55

Section 229.55 sets forth expedited recredit procedures applicable between savings associations. A claimant savings association must adhere to the timing, content, and form requirements of § 229.55(b) in order for the claim to be valid. A savings association against which an interbank recredit claim is made has ten business days within which to act on the claim (§ 229.55(c)). The provisions of § 229.55 may be varied by agreement. (No other provisions of Subpart D may be varied by agreement.)

Liability – § 229.56

Section 229.56 describes the damages for which a savings association or person would be liable in the event of breach of warranty or failure to comply with Subpart D. These damages include the following:

- The amount of the actual loss, up to the amount of the substitute check, resulting from the breach or failure.

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- Interest and expenses (including costs, reasonable attorney's fees, and other expenses of representation) related to the substitute check.

These amounts could be reduced in the event of negligence or failure to act in good faith. It is also important to note that § 229.56 has a specific exception that allows for greater recovery as provided in the indemnity section. Thus, a person that had an indemnity claim that also involves a breach of a substitute check warranty could recover all damages proximately caused by the warranty breach.

Section 229.56(b) excuses failure to meet this subpart's time limits because of circumstances beyond a savings association's control. Section 229.56(c) provides that an action to enforce a claim under this subpart may be brought in any United States district court. Section 229.56(c) also provides the subpart's statute of limitations, that is, one year from the date on which a person's cause of action accrues.⁵ Section 229.56(d) states that if a person fails to provide notice of a claim for more than 30 days from the date on which a cause of action accrues, the warranting or indemnifying savings association is discharged from liability *to the extent of any loss caused by the delay in giving notice of the claim*.

Consumer Awareness – §229.57

Content Requirements

A savings association must provide its consumer customers with a disclosure that explains that a substitute check is the legal equivalent of the original check and describes the consumer's recredit rights for substitute checks (§ 229.57). A savings association may, but is not required, to use the Board's model form (model C-5A in Appendix C to Regulation CC) to meet the content requirements for this notice. A savings association that uses the model form appropriately is deemed to be in compliance with the content requirement(s). A savings association may provide the notice required by § 229.57 along with other information.

A savings association must provide its consumer customers with a disclosure that explains that a substitute check is the legal equivalent of the original check and describes the consumer's recredit rights for substitute checks (§ 229.57).

Distribution to Consumers Who Receive Cancelled Checks with Periodic Account Statements

Under § 229.57(b)(1), a savings association must provide this disclosure to existing consumers who routinely receive their cancelled checks in their periodic statement no later than the first statement after October 28, 2004. For customer relationships established after that date, a savings association must provide the disclosure to a new consumer customer who routinely will receive cancelled checks in periodic statements at the time the customer relationship is established.

⁵ For purposes of this paragraph, a cause of action accrues as of the date on which the injured person first learns, or reasonably should have learned, of the facts giving rise to the claim, including the identity of the warranting or indemnifying savings association against which the action is brought.

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Distribution to Consumers Who Receive a Substitute Check on an Occasional Basis

Under § 229.57(b)(2), a savings association also must provide the disclosure to a customer who receives a substitute check on an occasional basis, including when:

- A customer receives a substitute check in response to a request for a check or a copy of a check.
- A check deposited by the consumer is returned to the consumer as an unpaid item in the form of a substitute check.

A savings association must provide the disclosure to a customer in these cases even if the association previously provided the disclosure to the customer.

When the customer contacts the savings association to request a check or a copy of a check and the savings association responds by providing a substitute check, the savings association must provide this disclosure at the time of the request, if feasible. Otherwise, the association must provide the disclosure no later than when the savings association provides a substitute check in response to the consumer's request. It would not be feasible to provide the disclosure at the time of the request if, for example, the consumer made his or her request by telephone or if the savings association did not know at the time of the request whether it would provide a substitute check or some other document in response. A savings association is not required to provide the disclosure if the association responds to the consumer's request by providing something other than an actual substitute check (such as a photocopy of an original check or a substitute check).

When a savings association returns a deposited item unpaid to a consumer in the form of a substitute check, the association must provide the disclosure along with the substitute check.

Mode of Delivery of Information – § 229.58

Section 229.58 provides that savings associations may deliver any notice or other information required under this subpart by United States mail or by any other means to which the recipient has agreed to receive account information, including electronically. A savings association that is required to provide an original check or a sufficient copy (each of which is defined as a specific paper document) instead may provide an electronic image of the original check or sufficient copy if the recipient agreed to receive that information electronically.

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REFERENCES

Code of Federal Regulations (12 CFR)

Part 229, Regulation CC, Subparts A – D

Closely Related Handbook Sections

[Examination Handbook Section 1335, Expedited Funds Availability Act](#)

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