

Basic Deposit Compliance
California Bankers Association
39th Annual Regulatory Compliance Conference

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D. FEDERAL REGULATORY AGENCIES of Financial Institutions (FI)

- a) Federal Reserve Board (Board of Governors of the Federal Reserve) (FRB)
- b) Office of Thrift Supervision (OTS)
- c) Office of the Comptroller of the Currency (OCC)
- d) Federal Deposit Insurance Corporation (FDIC)
- e) Federal Trade Commission (FTC)
- f) Financial Crimes Enforcement Network (FinCEN)
- g) Consumer Financial Protection Bureau (“CFPB”).

DEPOSIT OPERATIONS REGULATIONS

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I. Regulation CC - Check Availability and Collection [

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Basic Deposit Compliance

A Program in Two Parts

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This summary is not intended to express any legal opinions or to provide legal advice. You should consult an attorney for legal advice or review the law yourself.

INTRODUCTION TO DEPOSIT OPERATIONS

PART 1

A. DEPOSIT ACCOUNTS

1. What is the relationship between a financial institution (sometimes “bank” or FI”) and its customer?

Answer: Debtor – Creditor (The bank, as debtor, owes the accountholder, as creditor the amount of funds on deposit.) The bank is NOT a fiduciary to the depositor when the type of account is a regular deposit account.

2. What is the purpose of account documentation?

- Identify the accountholder and who is authorized to act on behalf of the accountholder
- Establish the contract between the bank and the accountholder

3. What is the contract between FI and the accountholder?

Bank documents

- Account application, agreement or signature card (“signature card”), which was a 4 by 6 card but now is more commonly a 8 ½ x 11 single or multi-page document
- Disclosure booklet(s):
 - i. **Account Agreement (Reg DD, E, CC)**
 - ii. Fee schedules, if separate from the disclosure book (Reg DD, E)
 - iii. Rate sheets (Reg DD)
 - iv. Privacy Policy (Reg P)
 - v. Supplemental/interim disclosures
- Any other FI agreement (trustee certification, power of attorney, cash management, wire transfer, etc.) executed by the accountholder.

Important note: Be concerned about regulatory issues that require “clear and conspicuous” disclosures.

The documents that define the contract are typically defined in the signature card and disclosure documents, e.g.,

Wells Fargo Consumer Account Agreement (4/15/2017) –

“This Agreement includes the following disclosures related to our consumer deposit accounts and related service that we have separately provided to you:

- The Consumer Account Fee and Information Schedule, which explains the schedule of our fees and other Account Related Information
- The Privacy Policy
- Rate sheets for interest-bearing accounts, each as modified by us from time to time
- Any additional disclosures regarding your Account that we may provide you.”

City National Bank Account Agreement and Disclosures (11/2016) –

“This Account Agreement and Disclosures document contains terms and conditions for the agreements that govern the deposit products and many of the banking services we make available to you as well as your use of these products and services and our facilities. This document, the fee schedule for the product or service you are using and any related agreement, disclosures or description we may provide you for a particular product or service make up our legal disclosure to you and are the agreement between you and us.

Accountholder documents

- Entity documents submitted by the accountholder (e.g., business identifying documentation, e.g., Articles of Incorporation, Fictitious Business Name Statement)
- Powers of Attorney
 - Statutory, bank form, or 3rd party prepared Power of Attorney
 - A power of attorney is a document that allows a person (the “principal”) to appoint a person or organization (Attorney-in-Fact or AIF or agent) to handle their affairs.
 - Important Note: ALL POWERS OF ATTORNEY TERMINATE on the DEATH OF THE PRINCIPAL.
 - Types of Powers of Attorney:
 - General power of attorney – a power of attorney in which the principal grants authority to the attorney in fact to carry out a wide variety of transactions.
 - Special or Limited power of attorney – a power of attorney in which the principal grants authority to the attorney in fact to do only specific, defined transactions.
 - Effectiveness of a Power of Attorney - durable/non-durable/springing
 - Durable power of attorney - a power of attorney that either becomes effective upon the incapacity of the principal or that survives the incapacity of the principal.

[Under *Probate Code* §4124 power of attorney must include either the following language or “similar words showing the intent of the principal”: (i) “This power of attorney shall not be affected by subsequent incapacity of the principal” or, if a springing power of attorney, a power of attorney contingent upon a future event, “This power of attorney shall become effective upon the incapacity of the principal.”
 - Non-durable power of attorney - a power of attorney that automatically terminates on the incapacity of the principal. NOTE: If the power of attorney does not contain the language of *Probate Code* §4124, the power of attorney is a non-durable power of attorney.
 - Additional information on Springing Powers of Attorney [*Probate Code* §4129] – a power of attorney that is effective upon the happening of an event e.g. incapacity of the principal. Section 4129 has provisions clarifying when a principal may designate one or more persons who can certify to the occurrence of the event that triggers the power of attorney.
 - Validity of Powers of Attorney [*Probate Code* §4121]
 - Created by natural person with capacity to contract [*Probate Code* §4120]
 - Must include date of execution
 - Must be signed by principal and
 - Principal’s signature notarized or witnessed by two persons (unless Financial Institution power of attorney under *Probate Code* § 5204)
 - if principal is current customer, may be liable for attorney’s fees incurred in action to confirm agent’s authority if FI refuses to accept [*Probate Code* § 4306]
- Trusts - An arrangement in which property is transferred to another to be held for benefit of someone or others.
 - There are three parties to any trust.
 - Trustor (or Settlor or Grantor) - This is the party who places the property into the trust relationship.

- Trustee - This is the party who receives the property from the trustor. The trustee holds and manages the property. A trustee has the powers granted by the trustor in the trust document or by law. A trustee owes a “fiduciary duty” to the beneficiary that the trustee will hold and manage property for the benefit of the beneficiary.
- Beneficiary - The person for whom the property is held.

Note: Quite often, one person (or, commonly, husband and wife) hold all three roles. E.g., John and Mary Smith are the Trustors; John and Mary name themselves as Trustees. During their lifetimes, John and Mary are the beneficiaries. After the last survivor is deceased, the property flows to their heirs – to be distributed by a successor trustee in accordance with the terms of the Trust document.

o Trustee’s Certification -

- In lieu of requesting the trust, Probate Code, §18100.5 provides the minimum requirements of a trustee certification. A trustee certification is valid if it:
 - contains a statement that it is signed by all of the trustees and is acknowledged (i.e. notarized); and
 - contains a statement that the trust has not been revoked, modified or amended in any manner which would cause the representations in the trustee’s certification to be incorrect.
- The Code provides that, additionally, the trustee certification may include:
 - A certification to the existence of the trust and the date of execution of the trust instrument;
 - Identity of settlor(s) and currently acting trustee(s)
 - Powers of trustee(s)
 - State the revocability/irrevocability of trust
 - Identity of person who may revoke the trust
 - If multiple trustees, signature authority of trustees (i.e., indicate whether all must act together, a multiple signature requirement, or if less than all trustees can act independently)
 - Provide the trust taxpayer identification number or Social Security Number
 - State the manner in which trust assets should be held

Contain the legal description of any interest in real property held in the trust.

▪ Deposit Account Control Agreements

- o Control agreement, where an FI client has borrowed from another lender. Under Commercial Code, Article 9, the lender and the depository institution must enter into an agreement whereby the depository institution agrees that the lender has “control” of the deposit account.
 - Control agreement cautions:
 - Can FI/is FI willing to do all that is required? Know your system limitations
 - Does the lender agree to indemnify FI, at least as to claims made for following lender’s instructions?
 - Can FI terminate the agreement?
- o Entity-specific legal documents: E.g., articles of incorporation or articles of organization (LLCs); certificate of limited partnership, LLC operating agreement, partnership agreement

BEWARE: REVIEW NON-FI PREPARED DOCUMENTS WITH GREAT CARE.

- Are all required language and any supplemental requirements (witness, notary, etc.) met?
- Are they consistent with the FI prepared documents?
- Does the FI (and internal FI management) understand what it is agreeing to do or not do? Do the FI's systems support the requirements or will the process be a manual one?

THE FI must do what it has agreed to do and so the FI must read, understand and verify compliance with everything the FI executes or otherwise agrees to.

- Does the entity have the proper number of signers in the signature card?
- Did you promise to restrict access to funds or monitor the account?
- Was a security interest created; is the system properly marked?

When in doubt, refer the documentation to an expert within the organization or to legal counsel. Better to have multiple eyes look at a document at the beginning than try to explain why the FI didn't follow instructions later or followed the instructions of a person acting under an invalid document.

5. CUSTOMER IDENTIFICATION PROGRAMS (CIP): What Documentation will the FI require to identify the accountholder and who is authorized to act on behalf of the accountholder?

See 31 C.F.R. §103.121 – Customer Identification Programs for banks, savings associations, credit unions, and certain non-Federally regulated banks.

See 31 CFR 1010.230 – Customer Due Diligence; Beneficial ownership requirements for legal entity customers (information gathering required beginning May 11, 2018)

- **Types of accountholders**
- Personal Accounts
 - Customer Identification Program:
 - name, date of birth, residential street address,
 - Identity must be verified through unexpired, government-issued ID (note type of document, ID number, place of issuance and date of issuance and expiration, if any) or verified through non-documentary methods (record methods employed);
 - TIN (for non-US person may accept passport number and country of issuance, alien id card or other government-issued document and, effective 1/1/18, new W-8s received will be require foreign owner's foreign TIN (FTIN) or a reasonable explanation for its absence -for example, country does not issue TINs. W-8s received prior to 1/1/18 will remain valid w/o FTIN until the earlier of 12/31/2018 or the expiration of the W-8 (Notice 2017-46)
 - Individual, Joint Tenant, Tenant-in-Common, Community Property
 - Tentative (Totten) Trust or Payable on Death Account
 - Alias: AKA/PKA Account
- Business Accounts
 - Customer Identification Program:
 - Name, physical address of principal place of business, local office or other physical address,
 - Identity must be verified through documents "showing the existence of the entity, such as certified articles of incorporation, a government-issued business license, a partnership agreement or trust instrument", non-documentary means, including public database or other source or, for non-US entities, alternative government-issued documentation certifying the existence of the business or enterprise;
 - TIN
 - Customer Due Diligence Requirements (information must be gathered 5/11/18 and thereafter.)

Written procedures are required.

Required for all “Legal Entity Customers”, defined as a corporation, limited liability company or other entity that is created by the filing of a public document with a Secretary of State or similar office, a general partnership, and any similar entity formed under the laws of a foreign jurisdiction that opens an account, with limited exceptions, primarily entities otherwise regulated and registered. Most significant of the exceptions are entities registered with the SEC, regulated financial institutions, public accounting firms registered under section 102 of the Sarbanes-Oxley Act, insurance companies regulated by the State, qualified nonprofits, and governmental entities.

Required each time a new account is opened. (We are awaiting clarification that the intent was not to require “each time” but rather that a risk-based approach may be used to determine how frequently the information shall be gathered—if within a particular period, no new certification is required.) Accounts include both deposit accounts and loans.

CDD requirements:

- Identify the beneficial owners of the legal entity—individuals who own, directly or indirectly, 25% or greater interest in customer.
- Identify a “single individual with significant responsibility to control, manage, or direct” the legal entity customer.

Information gathered must be verified, either through documentary or non-documentary review, except that photocopies of identification may be used in lieu of original documents.

A Model Certification Regarding Beneficial Owners of Legal Entity Customers is attached as Appendix A to §1010-230.

- NOTE: Account is defined broadly to include deposit accounts and loans of virtually all types. One compliance issue is where will the information be stored? For deposit accounts, it’s relatively easy—with the signature card. FIs generally don’t have a single location for credit/loan documents. One solution is to keep the documents with the other documents signed by the accountholder/borrower. Use of Fictitious Business Name
- Ownership Types
 - Sole Proprietorship
 - Partnership
 - Limited Partnership
 - Corporation
 - Limited Liability Partnership
 - Limited Liability Company
 - Non-U.S. Business Entity Not Doing Business in California
 - Unincorporated Lodges, Societies, or Associations
 - Charitable Organization
 - Attorney-Client Trust
 - Property Management Account
 - Coogan Minor Blocked
 - Insurance Fiduciary
 - Real Estate Brokers Trust
 - Estate (Administrators, Executors, Conservators, Guardians)
 - Revocable or Irrevocable Trust
 - Employee Benefit Plan

- Uniform Transfers to Minors Act (UTMA)
- Chapter 7 Bankruptcy
- Chapter 11 Bankruptcy
- Chapter 13 Bankruptcy
- Receivership
- Other account documentation/correspondence
 - Small estates: *Probate Code § 13100* Affidavit
 - *Financial Code §1450* Affidavit (previously 952)
 - Dispute letters-what can the FI do?
 - Requests for information
 - Coogan blocked account transfer/release request
- Helpful websites:

<http://www.leginfo.ca.gov/calaw.html> (for California Codes)

<https://businesssearch.sos.ca.gov/> (California Secretary of State for entity status verification and, as of 1/1/17, statement of information which identifies those authorized to act on behalf of the entity)

<http://www.lasuperiorcourt.org/civilCaseSummary/index.asp?CaseType=Civil> (Los Angeles Superior Court Civil Case index--Google other court websites. Different counties provide different amounts of information, some charge, others are free).

<http://scoweb.sco.ca.gov/UCP/> (California State Controller's unclaimed property website)

- <http://members.calbar.ca.gov/search/member.aspx> (California state bar attorney member search)

C. Death of an Accountholder

Personal

If a joint tenant, remaining joint tenant(s) are sole owners. If tenants in common or community property, heirs of decedent may have an interest. If last individual owner, property belongs to estate of decedent. When dealing with heirs, Letters testamentary/letters of administration are required. The will does not authorize the executor or heir(s) to receive funds. If the estate's value is \$150,000 or less, a small estate affidavit (*Probate Code § 13100* may be used.)

Practice tip: if you have a sole proprietorship which is an active business with employees, encourage the owner to add a "pay on death" beneficiary so the business is not interrupted pending appointment of an executor/administrator. (The authority of authorized signers ends with the death of the owner.)

Business

Businesses don't die but the death of officers, managers, members or partners may affect the ability of the business to transact business. Generally, the heirs become the owners of the corporation's shares owned by decedent and, if all of the owners, can elect a new board, appoint officers and execute a new signature card. Succession in the case of an LLC may be covered in the LLC's operating agreement and in the case of a partnership, in the partnership agreement. With statements of information which identify the parties authorized to act for an entity now being available from the Secretary of State, it should be easier to determine who succeeds a decedent.

C. Accountholder files for Bankruptcy

Will you freeze accounts pending instructions from the trustee/debtor in possession?

Chapter 7: Liquidation. Bankrupt debtor gives all non-exempt assets to trustee to distribute to creditors and gets a fresh start. Will you assume funds on deposit are exempt property of the accountholder? Accountholders often believe they get to keep everything and just wipe out their debts. Some banks have gotten into trouble for freezing and holding account funds for long periods of time without contacting the trustee. The individual debtor will not be opening up a Chapter 7 account. The bankruptcy trustee opens the bankruptcy account.

Chapter 13: Restructuring for persons with wages/income. Bankrupt debtor gives non-exempt assets and/or a portion of income to trustee to distribute to creditors and gets a fresh start. The individual debtor will not be opening up a Chapter 13 account. The bankruptcy trustee opens the bankruptcy account.

Chapter 11: Debtor in Possession ("DiP"). Bankrupt debtor has an opportunity to restructure debt, paying something (more than the creditors would have gotten in a Chapter 7 liquidation). The debtor needs a Chapter 11 DiP account. You cannot pay checks written by accountholder before filing without a Court Order. Everything written "pre-petition" (before filing for bankruptcy) must be returned "refer to maker" because that old entity is different from the new, DiP entity. Are you on the approved list of banks with the bankruptcy court? If not, you can't open a bankruptcy account. If you are, you can but are not obligated to open the account. Decide whether you want the business.

With automated payments, Courts are now allowing clients to simply re-title their old account by adding DIP but that can create problems for the bank. You still can't pay pre-petition checks. How are you going to monitor the account to be sure you don't pay pre-petition checks? If the client tells you it expects to use its old accounts, and they haven't been to court yet for authority to use old accounts (and there should be a specific order authorizing the use of old accounts), ask that they obtain a court order which includes something like:

1. Accountholder is authorized to continue to use its currently existing bank accounts
2. If applicable, Accountholder is authorized to use existing check stock, even though it does not contain the reference to "debtor in possession" or DIP (if they have a lot of check stock or expensive check stock, the court may let them use up the old stock. Alternatively, the court may let them use old stock but state they must stamp all checks, adding "debtor in possession" or "DIP".)
3. Crucial: Accountholder shall immediately provide bank with a list of outstanding pre-petition items which shall not be paid. Bank is authorized to pay any check issued by ABC not included on the list of "do not pay" checks.
4. If applicable, Accountholder is authorized to instruct bank to pay pre-petition checks/pre-petition payroll checks. Accountholder shall immediately provide bank with a list of outstanding pre-petition checks/pre-petition payroll checks which shall be paid. Bank is authorized to pay said pre-petition checks.

If the client simply has an order which authorizes it to continue to use old accounts, you will need more unless ALL pre-petition checks have been paid or the client provides a list of pre-petition checks which have not been paid and you are confident you have a complete list. If you pay a pre-petition check, the bankruptcy rule is that the funds are paid out of the bank's funds and the bank is then an unsecured creditor of the client for the amount of the check(s).

B. ARTICLE 3 & 4 OF THE CALIFORNIA COMMERCIAL CODE

Drawer	1001
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Andy Accountholder
123 California Street
New City, CA 90000
(213) 456-7890

01-123/1234

DATE _____

PAY TO THE
ORDER OF _____ \$ _____
_____ DOLLARS

Your Bank
132nd & California Office
123 Main St. STE 100
Los Angeles, CA, 90000
1-800-123-4567

FOR _____

: 1234123: 20100000000 01001

1. Definitions:

- Drawer – *Commercial Code* §3103(3) – Person who signs or is identified as the person ordering payment
- Drawee – *Commercial Code* §3103(2) – Person ordered to make payment
- Payee – Beneficiary of the payment
- Depository Bank – *Commercial Code* §4105(2) First bank to take an item; may be payor bank – unless item presented for payment over the counter
- Payor Bank – *Commercial Code* §4105(3) – Bank that is the drawee
- Negotiable Instrument – *Commercial Code* §3104 - means an unconditional promise or order to pay a fixed amount of money with or without interest or other charges if:
 - It is payable to bearer or to order at the time it is issued or first comes into the possession of a holder;
 - Is payable on demand or at a definite time
 - Does not state any other instructions but may give collateral and authority to dispose of collateral, confess judgment, or waive benefits of legal protections

2. Important UCC Rules

Drawer's Signature Missing/Forged (*Commercial Code* §§ 3401 & 3403)

A person is not liable on an instrument unless the person signed the instrument or the person's agent or representative signed the instrument. A signature includes one made by hand or machine, may be a mark or symbol and is binding so long as a person intended to authenticate the writing.

Unauthorized Signature (*Commercial Code* § 3403)

An unauthorized signature includes the absence of a signature where more than one is required on the part of an organization. Organization is defined broadly such that a joint tenancy account requiring two signatures would be included. An unauthorized signature may be ratified by conduct and express statements. This section was added in response to a California case which held that a bank could not take advantage of the various statutes of limitation discussed below because one of two required signatures was missing. Unfortunately, the amendment just addressed the specific concern—one of two

signatures missing, and did not consider whether no signature could be an 'unauthorized signature'. If a check is paid with no signature, the notice and statutes of limitation still don't apply. You can and should modify by terms and conditions of contract.

Endorsement Missing/Forged (*Commercial Code* §§ 3417, 4205, 4207 & 4208)

Warranties Upon Transfer/When Obtaining Payment (*Commercial Code* §§ 3416 & 3417, 4207 & 4208)

A person accepting a draft warrants the person is entitled to enforce the instrument; all signatures are authentic and authorized; the instrument has not been altered; and the person has authority to obtain payment.

Notice of a breach of warranty claim under these sections must be given within 30 days after the claimant has reason to know of the breach and the identity of the warrantor or liability is reduced to the extent the warrantor suffers loss caused by the delay.

Missing Endorsements (*Commercial Code* § 4205)

An FI is a holder of an item upon receipt if its customer was a holder of an item; it is not necessary to supply a missing endorsement to obtain holder status. In seeking payment of the item the depository bank warrants that it paid its customer.

Restrictive Endorsements (*Commercial Code* § 3206 a-c)

Most writings on a check which limit the right to indorse do not in fact affect the right to indorse or negotiate an instrument. In the absence of a valid restrictive endorsement, the payor bank and intermediary banks are not liable. "Pay A only" or "Payment due upon completion of work" are not effective to limit negotiation and the drawer is obligated to pay the item upon presentment. However, "For Deposit Only" is an effective restrictive endorsement and the instrument is converted by a purchaser, including the payor bank if the item is cashed when presented over the counter. "A in trust for B" may be paid according to its terms (that is, to the trustee in trust) unless one has actual notice of breach of fiduciary duty, in which case the check should not be accepted.

Restrictive Endorsements (*Commercial Code* § 3206(d) and § 3307)

To be liable for breach of warranty, actual notice of a fiduciary's breach must be held by the person taking the item. However, there is notice where the instrument is taken in payment of or as security for a debt known to be the personal debt of the fiduciary, is taken in a transaction known to be for the personal benefit of the fiduciary, or is deposited to an account other than an account of the represented person or a fiduciary account for the benefit of the represented person. A check payable to fiduciary drawn on an account on which one signs as a fiduciary (whether as trustee or corporate officer) may be cashed; the transaction, in and of itself, does not give rise to notice. However, a check payable to Corporation or trust, endorsed by an officer or trustee to self violates the section such that the Bank is not a holder in due course. Subsection (4) incorporates the *Sun `n Sand* duty imposed upon a bank to inquire of the drawer the purpose of a check payable to oneself.

Alteration (*Commercial Code* § 3407)

An alteration is an unauthorized change in an instrument. A bank taking an altered instrument for value, in good faith and without notice of the alteration may enforce the item according to its original terms or as completed if originally incomplete. It is legally acceptable to complete an incomplete item if one honestly believes completion is authorized (adding a date, for example).

30 Day Rule and One Year Notice Requirement /Customer's Duty to Review Statement (*Commercial Code* § 4406)

- **30 day rule**

A customer has a duty to review statements sent or made available to him. If the bank proves the customer failed to examine the statement and notify the bank with reasonable promptness (not more than 30 days), the customer is precluded from asserting its unauthorized signature or any alteration on the item if the bank also proves that it suffered a loss by reason of the failure. The customer is also precluded from asserting his unauthorized signature or alteration by the same wrongdoer on any later-paid item paid by the bank in good faith.

This section further imposes a modified comparative negligence test where the bank failed to exercise ordinary care. If the customer proves the bank acted in bad faith, the customer is not precluded from asserting later forgeries. If the bank proves the customer was negligent, fault and responsibility are assessed and liability split.

- **One year duty to notify**

Without regard to care or lack of care, a customer who fails to discover and report the customer's unauthorized signature on or alteration to an item is precluded from asserting the unauthorized signature or alteration.

One year time to file suit (*Code of Civil Procedure* § 340)

Suit must be filed within one year "by a depositor against a bank for the payment of a forged or raised check, or a check that bears a forged or unauthorized endorsement".

Three year Statute of Limitations (*Commercial Code* §§ 3118 (g) & 4111)

"An action (1) for conversion of an instrument, for money had and received, or like action based on conversion, (2) for breach of warranty, or (3) to enforce an obligation, duty, or right arising under this division and not governed by this section shall be commenced within three years after the cause of action accrues."

Limitations of Actions (*Commercial Code* § 4111)

"An action to enforce an obligation, duty, or right arising under this division shall be commenced within three years after the cause of action accrues."

Contributory Negligence (*Commercial Code* § 3406)

A party whose failure to exercise ordinary care contributes to an alteration or forged signature (burden of proof on bank) is precluded from asserting alteration or forgery against a person who takes item in good faith. If the bank fails to exercise ordinary care (burden of proof to prove this is on customer), the standard is comparative fault. A party has contributed to a forgery, for example, where he leaves a signature stamp with checks in an unlocked drawer, when it inadvertently mails check to wrong addressee with the same name as the payee, or she leaves blank spaces large enough to permit raising of the check. Failure to exercise ordinary care on the part of the bank may occur at the time of opening the account, especially if a large check is deposited to a new account.

Estoppel-Fraudulent Endorsement by Employee (*Commercial Code* § 3405) (Bad Bookkeeper Defense for FIs)

An endorsement by a person with authority to sign, endorse, process, provide information, control the disposition of checks, or otherwise act in a responsible role with respect to checks is effective as to a person who takes the item in good faith, exercising ordinary care. No proof of the employer's negligence is necessary. The employer is in the better position to stop the forgery. "Ordinary care is to be determined in the context of all the facts relating to the bank's conduct with respect to the bank's collection of the check." The bank's conduct in the opening of the account into which the check was deposited is

also considered. If account documents normally required are waived, the basis of the waiver must be documented as the issue may arise many years after the account's opening. (See Section 3406 above.) If the payee reasonably should have been known to the bank, it will be held liable.

Estoppel-Impostors/Fictitious Payees (*Commercial Code § 3404*) (Imposter Rule)

Where the payee is an imposter or agent of an imposter, the endorsement of any person in the name of the payee is effective in favor of a person who takes the item in good faith. An endorsement need only be "in a name substantially similar to that of the payee" or deposited into an account "in a name substantially similar. . . ." It does not have to be identical but it does need to be similar. A check payable to John Doe, endorsed Sam Smith and deposited to Sam's account is not subject to this section. However, if Sam signed John Doe and then Sam Smith, the section applies and the endorsement should be valid. The section affords protection only to one who pays **in good faith and exercises ordinary care**.

Charges Against an Account; Liability of Customer (*Commercial Code § 4401*)

The bank has the right to charge only "properly payable" items against the customer's account. Any check bearing a forged drawer's signature, a forged endorsement or alteration is not properly payable.

Recovery After Payment by Mistake (*Commercial Code § 3418*)

One has a right of recovery against a party paid by mistake unless the recipient took the check in good faith and gave value or changed his position in reliance upon payment. Mistaken payments include those made when the account was closed or there were not sufficient funds available. While the comment notes the winner is not clear in the case of a kite, it also may not be clear in the case of a creditor who receives a loan payment. Whether forbearance from collection is sufficient "value" is unclear and there may be a cause of action against the creditor/payee who received the check where it was paid by mistake.

Stale-Dated Checks (*Commercial Code § 4404*)

A bank is under no obligation to a checking account customer to pay a check (other than a certified check) that is presented more than six months after its date, but it may charge its customer's account for a payment made thereafter in good faith.

SUMMARY DISCUSSION

Remember, every case has two elements: liability and damages.

- Liability—did the bank do something wrong?
- Damages—did the accountholder suffer damages as a result of the FI's conduct?

Both elements must be present for an accountholder to have a possible claim against the bank.

Forged Drawer's signature

- The drawer's signature must be both forged and unauthorized. (If the accountholder authorizes a third party to sign the accountholder's name, the accountholder cannot later complain to the bank—the signature was authorized, even though it wasn't the accountholder's signature.)
- Each forgery has a one year statute of limitations—suit on the forged item must be brought within one year or the claim is time-barred.
- The accountholder holds the claim. If there is a dispute between partners, and one is claiming the other forged his signature or presented a check without his signature where two signatures are required, look closely at the issue of damages—was the accountholder (not the partner, but the business/acountholder) damaged.

- Has the accountholder suffered damage? If the forged checks paid debts of the accountholder, there is no damage and no liability. Accountholders have a hard time with this. They think they should get the face amount of the check back, even if they have suffered no damage.
- If an accountholder's failure to exercise ordinary care contributes to the making of a forgery or alteration, the accountholder is precluded from asserting the alteration or forgery against a person who, in good faith, pays the instrument. Checks left available to thieves, mail not delivered to a secure mail box, etc. may be grounds to deny liability.
- Additionally, banks should insist accountholders provide information concerning the forger. They don't get to recover from the bank while protecting their friend/relative.

Alteration/Missing-Forged Endorsement

- Alteration claims generally fall into two categories: altered payee and altered amount.
 - If the amount has been altered, the check can be enforced in its original amount. Example: check payable to John Doe for \$50 has been increased to \$500. Bank is entitled to \$50 and looks to John Doe for the \$450 difference.
 - If the payee has been altered, there is no right of payment on the check and the full amount is owed. Example: check was changed from John Doe to Sam Smith. The FI is entitled to nothing from the payor/drawee bank and must look to Sam Smith for recovery.
- Where an incomplete check is altered by completion, a bank taking the check in good faith and without notice of the alteration may enforce the check as completed.

Claims by the drawer against his/her/its bank

- A bank is authorized to charge against an account only those checks 'properly payable'. (§ 4401)
- An item is properly payable if it is authorized by the accountholder and properly indorsed. Thus a bank which charges an item bearing no or a forged endorsement (or is altered, as discussed above) has improperly charged the item against the account and is liable to the accountholder for damages unless the payee got benefit of the funds.
- Just as for forged drawer items, each forgery has a one year statute of limitations—suit on the item must be brought within one year or the claim is time-barred (CCP § 340).
- The 30 day rule (See § 4406) does not apply to missing/forged endorsements.
- The general negligence of the accountholder section does apply to missing/forged endorsements.
- Imposters and employee defalcations:
 - If an imposter induces a drawer to issue a check to a name the imposter provides, any endorsement in the name of the payee is effective as the endorsement of the payee if the item is taken in good faith. (Example: This is Mary from A Company, we haven't gotten payment on our last invoice. Please send your check to 123 Main. Regardless of whether Accountholder owes A Company any money, when it sends its check to 123 Main, Mary's address, anyone can endorse the check.) This rule applies only if the person taking or paying the check exercised ordinary care.
 - If a person authorized to sign checks issues a check with no intent that the payee receive it, any endorsement in the name of the payee is effective. (Example: John, treasurer and authorized signer of accountholder, issues a check payable to Mary Smith. Regardless of whether Mary is owed any money, if John intended to steal the proceeds of the check at the time he signed it, any endorsement is effective.) This rule applies only if the person taking or paying the check exercised ordinary care.
 - If an employee has the responsibility to (a) sign or endorse checks on behalf of the employer or to (b) process checks for deposit payable to the employer, or to (c)

prepare or process checks for issue in the name of the employer, or to (d) supply the name or address of the payee or to (e) control disposition of the check or to (f) act otherwise in a responsible capacity, the employer bears the loss as against a claim by a person who takes or pays the item in good faith and while exercising ordinary care. (Examples: bookkeeper is to endorse company checks for deposit but endorses and deposits checks to his own account, supplies the name of payees and provides a fictitious payee, cashing the check, or supplies his own address coupled with name of genuine payee so that the check is sent to the bookkeeper who can then cash the check, in each case, if the bank paid in good faith and exercised ordinary care, the loss falls on employer.)

In each of these cases the bank must have paid in good faith and exercised ordinary care. Additionally,

Right of indemnification against bank of first deposit

- While the payor/drawee bank is liable to its accountholder for a check paid with a forged or missing endorsement, it has a claim against the bank of first deposit for breach of warranty. By presenting the check for payment, the bank of first deposit (warrantor) represents to the payor/drawee bank that the warrantor is entitled to enforce payment. The bank of first deposit is entitled to enforce payment only if the payee got the money, but there are defenses.
- When did the accountholder report the forgery to the payor/drawee bank? If the payor/drawee bank waits more than 30 days prior to giving notice to the warrantor, the warrantor is discharged to the extent of any loss caused by the delay in giving notice of the claim. (Since forgers usually spend money as fast as it is stolen, delay often does not matter.)
- The payor/drawee bank is obligated to assert all defenses available to it, including the accountholder's negligence.
- As in any case, what seems a clear-cut, valid claim for breach of warranty can be denied by the FI which breached its warranty. The payor/drawee bank then has the option of suing the bank of first deposit for the face amount of the item if it has reimbursed its accountholder. Attorneys' fees are not recoverable in California. Some banks, especially out-of-area banks, will deny what appear to be obvious claims in the hope that the payor/drawee bank will not sue.

Note: Where a check has both a forged drawer's signature and a forged endorsement, the payor/drawee bank is liable.

Important Rules Regarding Remotely Created Checks (also called Demand Drafts).

Defined: Commercial Code § 3104(k) as "a writing not signed by a customer that is created by a third party under the purported authority of the customer for the purpose of charging the customer's account with a FI. A demand draft shall contain the customer's account number and may contain any or all of the following:

- (1) The customer's printed or typewritten name.
- (2) A notation that the customer authorized the draft.
- (3) The statement "No Signature Required" or words to that effect.

Traditionally, the drawee bank would be responsible to its client if the demand draft were not authorized. Due to the realities of automated clearings, the liability for unauthorized drafts is on the depository institution which is in the best position to monitor for authority by "knowing its customer." See Regulation CC 229.34 § (d)

"Transfer and presentment warranties with respect to a remotely created check.

(1) A bank that transfers or presents a remotely created check and receives a settlement or other consideration warrants to the transferee bank, any subsequent collecting bank, and the paying bank that the person on whose account the remotely created check is drawn authorized the issuance of the check in the amount stated on the check and to the payee stated on the check. For purposes of

this paragraph (d)(1), “account” includes an account as defined in § 229.2(a) as well as a credit or other arrangement that allows a person to draw checks that are payable by, through, or at a bank.

(2) If a paying bank asserts a claim for breach of warranty under paragraph (d)(1) of this section, the warranting bank may defend by proving that the customer of the paying bank is precluded under U.C.C. 4-406, as applicable, from asserting against the paying bank the unauthorized issuance of the check.

HOT TOPIC: Order of Payment of Checks and Other Items.

C. **LEGAL PROCESS (A BRIEF Summary)**

In this section, the California Code of Civil Procedure is called by the initials “CCP”; Internal Revenue Code is called by the initials “IRC”.

Who may issue a legal process:

- Courts
- Governmental administrative agencies
- Law enforcement
- Extra-judicial officers (arbitrators, etc.)

From where might a legal process be issued

- California
- A state other than California
Note: State legal process from a state other than California is rarely valid, except where you are a multi-state bank
- The Federal Court System (including Bankruptcy courts)

What may be included

- A demand for funds (usually through a levy or attachment)
- A demand for documents (usually a subpoena)
- A demand that action be taken or not taken (usually a temporary restraining order (TRO) or preliminary injunction)

DEMANDS FOR FUNDS—WRIT OF EXECUTION/LEVY OR ATTACHMENT

1) **California Writ of Attachment**

A writ of attachment is a process by which a party to a lawsuit can tie up funds of another party while the suit is going on in anticipation of a successful result after trial. That way there is something to recover when the party is successful. A Writ of Attachment prevents the owner of the funds from spending the funds. In responding to a Writ of Attachment, FI can either hold the funds while the suit is going on or pay the funds to the sheriff to deposit with the court. The lawsuit could go on for a long time. Consider whether you want responsibility for keeping track of the funds for a long time and trying to figure out to whom to give the funds after the attachment expires and you or the customer has closed the account and left no forwarding address. Consider whether the funds should be held in an interest-bearing account (even if not in an interest-bearing account at the time of service).

Documentation Requirements

- Notice of Attachment [CCP § 488.060]
- Writ of Attachment [CCP § 488.010]
- Memorandum of Garnishee [CCP § 488.610]

- 2) **California Writ of Execution/Levy.** A writ of execution and levy is one process by which a successful party seeks to collect money from a judgment debtor. It is used when the property sought is held by third parties.

Documentation Requirements

- Notice of Levy. [CCP § 699.540]
- Writ of Execution. [CCP §§ 699.510; 699.520]
- Memorandum of Garnishee. [CCP § 701.030]

3) **Processing California Writs of Execution and Levy or Attachment**

- a) Determine whether service requirements were met:
- personal service
 - at your designated centralized location. (You must designate a centralized location if you have more than 9 branches in the state. If subject to mandatory rule and no centralized location designated, service at any branch effective. You may require service on branch of account for safe deposit boxes if you so indicate. CCP 684.115)
 - served by a levying officer: Sheriff, marshal or constable [CCP § 680.260] Registered process server [CCP § 699.080(a)(5),(6)]
 - Copy of Writ & Notice served on co-owners. [CCP § 700.140]
- b) Identify **whose** funds are to be held
- Look at the *Writ* of Attachment/Execution to determine who the debtor(s) is/are.
- c) Identify **what** funds are to be held
- (1) Look at the *notice* of attachment/levy to determine which debtor(s) is/are covered and what funds or other property of that debtor are to be held.
 - (2) Unless there is a specific court order, the notice cannot expand whose funds are to be taken; the accountholder must be listed on the writ as a debtor in order for the accountholder's property to be subject to levy.
 - (3) The notice of attachment/levy may seek less than all of the property of all of the judgment debtors.
 - (a) A party who seeks all of the debtor's property will usually use language such as "any and all property of debtor held by you" or "any and all accounts of debtor held by you", or words of similar effect. Property includes safe deposit box contents. Accounts includes only deposit accounts. To steer the bank holding property in the right direction, the legal process description of property to be levied upon may go on to say: "including, but not limited to, account number XXX".
 - (b) Either because the party seeking the debtor's property only wants to reach a particular account, or due to poor drafting, the legal process may be limited. For example: if the notice of levy says "execute on account number XXX", only account number XXX is reached, even if the accountholder has a lot of money in another account. Additionally, be sure the specific account identified is property of a debtor. (Either because the creditor is overreaching or due to an innocent mistake in listing an account number, a third party's account may be identified. Except in limited instances, a third party's account can be reached only with a court order.)
 - (4) Only property which belongs to a debtor **and** is asked for by the levying party is covered by the levy.
- d) What is the **amount sought** - The legal process often includes an interest factor which must be calculated. Remember to calculate interest through the date of the payment.

- e) Identify funds subject to levy.
- i) If the FI fails to hold funds which were subject to levy, the bank may be liable to the judgment creditor.
 - ii) Determine whether the funds in an account are automatically exempt: If social security or other public benefits are directly deposited to the account, then funds are automatically exempt from the levy under State and Federal law. The greater exemption applies. [CCP § 704.080 and 31 CFR 212.3]
 - CCP
 - (a) \$1,225 – single designated payee of public benefits
 - (b) \$2,425 – single designated payee of social security
 - (c) \$1,825 – multiple designated payees of public benefits
 - (d) \$3,650 – multiple designated payees of social security
 - (e) CFR
 - CFR

The lesser of all benefit payments posted to an account between the close of business on the beginning date of the lookback period and the open of business on the ending date of the lookback period. Lookback period means the two month period that begins on the date preceding the date of account review and ends on the corresponding date of the month two months earlier, or on the last date of the month two months earlier if the corresponding date does not exist. (This means there may be 2 or 3 months of payments which are exempt. Calculations are complicated and you may want to involve counsel. Also, see the examples in the CFR.
 - iii) Other property may be exempt but customer must file a claim of exemption as to potentially exempt property.
 - (1) A list of exempt property is found at CCP §§ 704.010 – 704.210.
 - iv) Determine whether the funds in an account are subject to a banker's lien.
 - (1) If the debtor owes the FI money on a matured debt, except in the case of an IRS levy, the FI may assert a senior claim to the funds.
 - (2) Prior legal process (for example a pending attachment hold followed by a levy by another creditor) may create a senior right to funds.
 - (3) A deposit account control agreement, tri-party lockbox agreement, or other agreement may give a third party a security interest in an account. If a security interest or other non-judicial lien is reflected on the account remarks, be sure the senior lienholder is notified so that it can take appropriate action. The senior lienholder may petition the Court for a determination that its lien is senior/superior to the levying party. If there aren't other monies to attach/levy upon, the current legal process may become a junior lien. FI must note the fact that a junior lien has been created in the comments section of account remarks and, if the senior lien is released process the later-served legal process. Levy on deposit by writ of attachment or writ of execution creates lien. [CCP §§ 488.500 and 697.710]. Attachment lien lasts for 3 years from date writ issued, with one-year extensions, up to total of eight years. [CCP § 488.510]. Execution lien lasts for 2 years from date writ issued. [CCP § 697.710]. Bank should record and log date of service of writs on deposits which are then subject to

security interest in favor of FI, a third person [UCC § 9302(1)(g)] or other writ (e.g. attachment) served by prior creditor in the event the earlier lien terminates or is released prior to termination of junior lien.

- v) In cases where a debtor has multiple accounts, one possible order of taking is:
 - (1) Money specifically identified in a Court order, if so specified in the levy/attachment.
 - (2) Money from non-exempt accounts in the debtor's individual name, alone. Where there are multiple debtors, take money from accounts held jointly by the debtors.
 - (3) Money not clearly exempt from accounts in the debtor's individual name, alone. Where there are multiple debtors, FI may want to take money not clearly exempt from account held jointly by the debtors.
 - (4) If an unexpired copy of a fictitious business name statement was served with the legal process, take money from an account held in the name of a fictitious business owned by a debtor. (Note: a copy of the fictitious name statement is not required if the business is a judgment debtor.)
 - (5) Money from non-exempt accounts, and then accounts with possibly exempt funds (leaving statutorily exempt funds on deposit) held jointly by the debtor(s) and their spouses.
 - (6) Money from non-exempt accounts, and then accounts with exempt funds (leaving exempt funds on deposit) held jointly by the debtor(s) and third parties.
 - (7) If an affidavit of spouse was served with the legal process, take money from an account belonging to a spouse, alone or with third parties. (Note: An affidavit of Spouse is not required if the property is held by the debtor and his/her spouse—see (5) above.)
- vi) If there are insufficient funds to satisfy the levy from 1-7 above, and the legal process was served before the bank's cutoff hour for legal process (which can be no earlier than one hour after the branch's opening), determine whether any of the accounts held had debits post against the account which can be timely returned. Return the debit transactions and hold the funds subject to legal process.
- vii) If the accountholder asks that another order of taking funds be applied, and there is no exposure to the FI in complying, the accountholder's request may be honored. Be sure you review the accounts and request to avoid exposure to the bank.
- viii) If, after taking funds from all deposit accounts, additional monies are owed, determine whether the legal process reaches safe deposit boxes.
 - (1) If safe deposit box(es) is/are subject to the legal process, seal or otherwise restrict access to the box(es).
 - (2) Return the Memorandum of Garnishee stating that a box is being held. Advise if the box is in the name of the judgment debtor and

another person or persons. State the name and address of the other person(s).

- (3) Allow access to the levying officer when notified to do so by the levying officer.
- ix) If box forcing is required, the bank is entitled to the repair cost in advance. [CCP § 700.150(d)]
- x) If FI have sufficient funds to satisfy the levy, hold them as required by law and remit when the time to remit is due. No Memorandum of Garnishee is required.
- xi) FI should complete and return the Memorandum of Garnishee if:
 - (1) FI are unable to comply. State a reason under item number 1.
 - (2) FI are unable to fully comply. State the amount you are holding and a reason why you can't fully comply under item number 1.
 - (3) FI are holding a safe deposit box. Confirm that item number 5 of the Writ of Attachment instructs the FI to hold a safe deposit box. If so, identify the box being held.
 - (4) The account or safe deposit box being held is in the name of the defendant and another person or persons. State the name and address of the other person(s).
 - (5) FI are holding an amount in excess of Social Security Direct Deposit exemptions. State the amount.
- xii) Remit the funds being held to the levying officer with the memorandum of garnishee, if applicable.
 - (1) Remit the funds to the sheriff, marshal or constable. Do not remit funds to a registered process server.
 - (2) If the account being held is in the name of the judgment debtor alone, remit in 10 days.
 - (3) If the account is in the name of a person other than the judgment debtor, whether alone or with the judgment debtor, remit when notified to do so by the levying officer (at least 15 days after service).

4) **Selected compliance issues**

- a) Levies on Express Private Trusts. An express private trust is a trust created by a trust agreement.
 - i) If the trust is the debtor, trust property is reached.
 - ii) If a trust beneficiary is the debtor, trust property is generally not reached. CCP Section § 699.720(a)(8). A Court order (generally from the Probate Court) is required to reach the beneficiary's interest in trust property. CCP Section § 709.010(b).
 - iii) If the settlor retains the power to revoke the trust, trust property is subject to the claims of creditors of the settlor to the extent of the power of revocation.
- b) Levies on Guardianship and Conservatorship Estate Accounts are reached by a court order issued by the Probate Court where estate is pending. The account is not subject to levy by writ of execution or other "civil" charging order. [CCP § 709.030]
- c) Handling Levies on Professional Trust Accounts.
 - i) General Rule: "The creditor of a bank depositor who garnishes money in the bank to the credit of his debtor is in no better position than the depositor. Consequently, funds cannot be attached or garnished in an action against the depositor where they

have been deposited in trust or belong to another. Thus, money deposited in a bank in the name of an individual, followed by the word 'agent' or 'trustee' or other words suggesting that the depositor is acting as agent or fiduciary for a third person, cannot be garnished as funds of the depositor where it is proved that the depositor did not own the funds but was acting for another. But if it is not proved that the depositor is not in fact the owner of the deposit, he will be treated as the owner and the deposit may be garnished to pay his debt. Funds actually belonging to a debtor but deposited in an FI in the name of a third party, may be reached by his creditors by garnishment."

- ii) Escrow Trust Account Exemption [*Financial Code* § 17410]
 - (1) Exempts escrow agent trust accounts from enforcement of money judgment procedures, for claims against the escrow agent licensee.
 - (2) Applies only to escrow agents licensed by the California Commissioner of Corporations.
- iii) Attorney-Client Trust Accounts are not automatically exempt. This is because an attorney-client trust account is not held by a "trust" as defined in Section 82, and because the bank cannot determine whether the funds in such an account belong to the attorney or to clients. (For example, a dishonest attorney could attempt to shield assets from levy by holding funds in such an account. An honest attorney may have an ownership interest in funds on deposit through a contingency fee agreement). The attorney-client trust account may be levied if the account is in the name of the judgment debtor (the attorney/law firm). The Internal Revenue Service, Franchise Tax Board, State Board of Equalization, and Employment Development Department take the position that their levy reaches attorney-client trust accounts. If an attorney complains, instruct him/her to obtain the written consent of the levying party's attorney to release the funds.
- iv) Other Professional/Trade Trust Accounts: Groups are sometimes successful in having their trust funds declared exempt. If an accountholder claims an exemption exists, ask for the code section. Review the code section to see if you agree or refer the matter to your attorney for review.
- d) Account Misdescription: If the difference between the name of the debtor and the accountholder is "the result of a technical misdescription," and the FI has reason to believe that the account holder and the debtor are the same, funds should be held. If there is an issue whether to hold funds due to a misdescription, contact legal counsel.

5) **United States District Court Writs of Execution**

- a) Are issued pursuant to Federal Rule of Civil Procedure 69, which provides that they shall follow state law where the court is located (here, California), except to the extent there is a federal law which takes precedent.
- b) Documents served:
 - i) Federal writ of execution
 - ii) California Notice of Levy
 - iii) California Memorandum of Garnishee

6) **Internal Revenue Service Levies** (IRC 6331 et seq.; 26 CFR 301.6331 et seq. and 26 CFR 301.6332-3 (Final Regulation, 58 Fed. Reg. 16, January 4, 1993.))

- a) Documentation required: Notice of Levy
- b) Compliance Procedures

- i) Notice of Levy applies to funds on deposit at the time the levy is made, up to the amount of the levy.
- ii) Bank must hold funds for 21 calendar days, remitting the funds held on the first business day following the 21st calendar day after the levy is made, absent a Release of Levy, or a notice of an extension of the holding period.
- iii) If the account is interest-earning and the balance being held is insufficient to fully comply, the interest earned during the hold period goes to the IRS. In no event, however, must the FI remit an amount greater than the amount of the levy.
- iv) Depositor may waive the 21-day holding period. If a multiple ownership account, all owners must agree to the waiver.
 - (1) Note: Bank may want to wait at least 10 days since last non-cash deposit for returns.
- v) Individual Retirement Accounts are generally exempt, but the IRS may attach an IRA by agent signing the signature block to the right of the exemption statement on the levy.
- vi) Bank may not deduct a processing fee from the amount being held if the amount remitted is less than the levy, but may assess a regular transaction or withdrawal charge if such a charge could be imposed on the customer in connection with a withdrawal by the customer.
- vii) Bank may apply the early withdrawal penalty on certificates of deposit if maturity is after the required remittance date.
- viii) Only bases for bank not remitting funds are (a) no property of taxpayer held, or (b) property subject to a judicial lien (for example, prior state attachment). If property is subject to a non-judicial lien (e.g. security interest) bank should contact IRS for instructions (and notify secured party). If IRS insists funds be remitted, FI may consider interpleader or remit funds and secured party institutes and action against IRS for recovery of funds. Unreasonable failure to remit could subject to a penalty equal to 50% of amount of property. [IRC § 6332(d)(2)] See U.S. v. Trans World Bank (1974) 382 F. Supp 1100 (C.D. Cal).

7) Franchise Tax Board Order to Withhold or Warrant for Collection

- a) Documentation Required: Order to Withhold
- b) Compliance Procedures.
 - i) Notice of Levy applies to funds on deposit at the time the levy is made, up to the amount of the levy unless the levy is continuous. If continuous, obtain legal advice
 - ii) Hold funds for 10 business days, then remit.
- c) State Board of Equalization (“SBE”) Levy
 - i) May issue in one of three forms:
 - ii) Notice to Withhold [Rev & Tax § 6702]
 - (1) Hold the funds for 60 calendar days. Notify the State Board that FI is holding funds. Release funds after 60 days unless served with Notice of Levy, consent to transfer from SBE, or Warrant for Collection.
 - (2) SBE may cause to be withheld up to twice the amount due it, including interest and penalties.
 - (3) Notify the SBE and each person named on account(s). FI may charge reasonable fee for notice to depositor, not in excess of \$3/notice.
 - iii) Notice of Levy [Rev & Tax § 6703]

- (1) Hold the funds for 10 calendar days, then remit the funds to the State Board.
- iv) Warrant for Collection [Rev & Tax § 6776]
 - (1) Should be treated as a writ of execution. [CCP § 995.220]

DEMANDS FOR RECORDS — SUBPOENA

- 8) OVERVIEW: In order for a subpoena to be issued, there must be a lawsuit pending. The subpoena will command the appearance at a deposition either with or without records, or it may call for records only. If the subpoena is valid, production according to the date specified in the subpoena is required unless otherwise agreed.
- 9) CALIFORNIA CIVIL SUBPOENA
 - a) HOW SERVED.
 - i) Personal service
 - ii) On a FI officer, director, custodian of records or anyone else authorized to accept service. (CCP § 1987) Be sure receiving employees review the subpoena to determine to whom the subpoena is directed if you don't want them accepting service on behalf of an employee. (Should a subpoena requiring appearance of Edward Employee be served on Edward or any authorized bank employee?)
 - b) WHAT IS SERVED.
 - i) SUBPOENA
 - (1) Signed by the court clerk, judge, or the attorney of record. (An *in pro per* person representing self, cannot sign and issue a subpoena unless (s)he is an attorney. (CCP § 1986)
 - ii) APPEARANCE (DEPOSITION OR TRIAL)? A copy of the affidavit upon which the subpoena is based must be served with the subpoena. (CCP § 1987.5) Note: If personal appearance is required, consult legal counsel. Do you want an attorney representing the witness? Especially in a deposition, the bank's representative may be lead down the garden path to admitting the bank was negligent or otherwise at fault and then the bank is added as a defendant with an admission of fault already established.
 - iii) CONSUMER RECORDS? Notice to Consumer or Written Authorization by Consumer (CCP § 1985.3)
 - (1) "Consumer" means any individual, partnership of five or fewer persons, associations or trusts. (CCP § 1985.3(a)(2)) LLCs are not consumers, even if only one member and a disregarded entity using the member's TIN.
 - (2) If more than one consumer owns an account, a proof of Notice for each consumer/owner is required.
 - (3) It is the responsibility of the requesting party to determine who all the joint consumer/owners are. The subpoenaed party should not disclose the identity of joint consumer/owners.
 - c) WHEN SERVED
 - i) If Consumer records
 - (1) Timing of service on the consumer: The requesting attorney must serve the Notice on the consumer at least 5 days before service upon the witness. If notice served on the consumer by mail – add an additional 5 days. If served by overnight courier – add 2 days. (CCP §§ 1985.3(b)(3) & 1013)

- (2) Timing of service on the witness: Service on the witness must be at least 10 days before the production date specified in the subpoena. (CCP § 1985.3(b)(2)) NOTE: If a deposition subpoena is served, CCP § 2020(d) provides that the subpoena may command compliance no earlier than 20 days after issuance or 15 days after service.
 - ii) If non-consumer records
 - (1) No earlier than 20 days after issuance or 15 days after service, unless the court orders a shorter time.
 - iii) If for non-consumer records and appearance at trial or deposition
 - (1) the subpoena need only be served to allow a reasonable time to gather the records and travel to the noticed site.
 - d) BRANCH RESPONSIBILITIES
 - i) Notations: The branch should note legibly on the face of the subpoena: (1) date served; (2) manner of service; (3) branch served; (4) employee receiving service; (5) signature of employee receiving service.
 - e) SUBPOENA PROCESSING'S RESPONSIBILITIES
 - i) Verify validity of service and subpoena.
 - (1) Manner of service.
 - (2) Required documentation - Consumer?
 - (3) Proper form and all required signatures.
 - ii) Notify primary customer(s) of subpoena.
 - iii) Identify what is being sought in the subpoena
 - (1) Appearance? Notify appropriate department regarding the appearance. The date of the appearance may need to be modified depending upon records sought.
 - (2) Scope of records sought. The subpoena must describe with reasonable certainty the records being sought.
 - (a) Name of customer
 - (b) Specific accounts?
 - (c) Time frame?
 - (d) POINTER: Account records may be destroyed after the period set by FI record retention policy (Since the Bank Secrecy Act requires a five-year retention period, generally your records will be retained for at least five years). If the time frame sought is nearing the destruction date, focus retrieval on the oldest records.
 - (3) Specific records: statements, deposits vs. deposit slips, checks, withdrawals, offsets, wire transfers, etc.
 - iv) Contact Requesting Party – If necessary, request a limitation of scope or request an extension. If requesting party is unwilling to limit an overly broad subpoena or grant an extension to produce, contact a supervisor. Ultimately, legal counsel may be needed.
- HELPFUL HINTS:
- (1) If seeking to limit the scope: Generally it helps to know the volume of records subject to an overly broad subpoena. FI will likely need to retrieve statements first. Provide the requesting party with the estimated costs for such production. Do not disclose (e.g., fax) copies of the statements prior to

the production date. Ask what records he/she is hoping to find. FI may need to provide guidance in limiting the scope. Whatever is agreed to, it is best to confirm understandings in writing.

- (2) Time extensions: Suggest a staggered production according to the requesting parties needs, by month, dollar, account, etc. First production must occur after the production date specified in the subpoena unless the account holder agrees otherwise.
- (3) Promptly communicate unfavorable developments. Failure to timely communicate problems relating to a retrieval often results in a more costly solution. Regularly check the status of retrievals as the due date approaches. If the status indicates a problem, there may be a need to escalate the issue to a supervisor and/or legal counsel.

v) CUSTOMER OBJECTIONS

- (1) PARTY or Non-Consumer: Must bring a motion to quash or modify the subpoena.
- (2) NON-PARTY Consumer: Serve on the requesting party and the witness a written objection stating the specific reasons why the records should not be produced. (CCP § 1985.3(g))
- (3) STAY PRODUCTION: Upon notice that a motion has been filed, or receipt of written objections from a non-party consumer, the witness may cease production of records until ordered by the court to do so.

vi) FAILURE TO APPEAR.

- (1) GENERAL: If the bank fails to appear and/or to produce documents (for whatever reason) and the requesting party believes that an appearance and/or production is still required, the requesting attorney generally will file a motion to compel production. The requesting attorney generally will seek court costs and attorney's fees associated with such action.
- (2) CALIFORNIA PENALTIES:
 - (a) Protective/Compel order: If the subpoena is objectionable and the subpoenaing party will not agree to amend the subpoena, e.g., change the date of production or scope of records sought, the witness must seek the protection of the court. Conversely, if the witness refuses to comply with a subpoena, the requesting party can seek an order from the court compelling production. (CCP § 1987.1)

NOTE: The subpoena must give the witness a "reasonable time" to locate and produce the records. (CCP §§ 1985.3(d) and 2020.220)
 - (b) \$500 penalty: The requesting party may seek to recover \$500 and all damages sustained if a witness fails to appear as required by a subpoena. (CCP § 1992.)
 - (c) Bench warrant: The court may issue a warrant to arrest the witness and bring the witness before the court. (CCP § 1993).

vii) PRODUCTION:

- (1) AFFIDAVIT OF CUSTODIAN: The custodian must state: (1) the affiant is qualified to certify the records; (2) copies are true and correct; (3) records were prepared in the ordinary course of business; (4) identity of the records; and (5) mode of preparation. (Evidence Code § 1560)
- (2) PACKAGING: Records shall be separately enclosed in an inner sealed envelope which is marked with the title and case number, name of the witness, and date of the subpoena. (Evidence 1560(c))

NOTE: Unless the parties agree otherwise, the records are to remain sealed and shall be opened only at time of trial, deposition, hearing, or as ordered by the court. (Evidence § 1560(d))

- (3) COSTS: The witness is entitled to recover “reasonable costs” incurred in responding to the subpoena.

\$0.10/page - Standard copies

\$0.20/page – Copies from microfilm

Actual costs for oversize documents or documents requiring special processing

\$24/hour (\$6/quarter-hour) – reasonable clerical costs incurred in locating and making records available. Evidence Code § 1653(b)(1).

- (4) C.O.D.?: Occasionally, sending records C.O.D. may be appropriate. Consider C.O.D. if: the requesting party has a history of unpaid invoices; the production is large; or attorney has been uncooperative. The FI cannot require payment prior to retrieval, but may demand payment simultaneously with actual delivery. Evidence Code § 1563(b)(2).

b) FEDERAL CIVIL SUBPOENA, including Bankruptcy Court Subpoenas

c) Federal Courts have nationwide jurisdiction. In other words, a subpoena issued out of a court in Georgia may still be served upon your FI in California. The production location shall be no more than 100 miles from the producer’s location. A motion to quash does not stop production; a court order is required to stop production.

The reasonable costs for Federal agency and civil subpoenas – See Federal Reserve Board Regulation S, § 219.3 Fees payable by a government authority seeking access to financial records pertaining to a customer, by written request, through:

(i) A court order;

(ii) A subpoena issued pursuant to the Federal Rules of Criminal Procedure or the Federal Rules of Civil Procedure; or

(iii) Other agency administrative procedures, including administrative subpoenas, voluntary requests, or other process shall reimburse the financial institution for reasonably necessary costs directly incurred in searching for, reproducing or transporting books, papers, records, or other data as set forth in this section.

Appendix A to §219.3—Reimbursement Schedule

Reproduction:	
Photocopy, per page	\$0.25
Paper copies of microfiche, per frame	0.25
Duplicate Microfiche, per microfiche	0.50
Storage media	Actual cost.
Search and Processing:	
Clerical/Technical, hourly rate	22.00
Computer Support Specialist, hourly rate	30.00
Manager/Supervisory, hourly rate	30.00

2) CALIFORNIA CRIME REPORTS

California Government Code 7480(b) - Requires banks to release specific information when any California police, sheriff's department, district attorney, county protective services office, long-term care ombudsman provides a written certification that a crime report has been filed that involves the alleged fraudulent use of drafts, checks, access cards, or other orders drawn upon any California bank, or when investigating financial abuse of an elder or dependent adult. The FI must furnish a statement setting forth the following information with respect to a customer account specified by the requesting party for a period 30 days prior to, and up to 30 days following, the date of occurrence of the alleged illegal act involving the account:

- (1) The number of items dishonored.
- (2) The number of items paid that created overdrafts.
- (3) The dollar volume of the dishonored items and items paid which created overdrafts and a statement explaining any credit arrangement between the bank, credit union, or savings association and customer to pay overdrafts.
- (4) The dates and amounts of deposits and debits and the account balance on these dates.
- (5) A copy of the signature card, including the signature and any addresses appearing on a customer's signature card.
- (6) The date the account opened and, if applicable, the date the account closed.
- (7) Surveillance photographs and video recordings of persons accessing the crime victim's financial account via an automated teller machine (ATM) or from within the financial institution for dates on which illegal acts involving the account were alleged to have occurred.

The law expressly provides that providing one or more complete account statements is proper compliance.

INTRODUCTION TO DEPOSIT OPERATIONS

PART 2

REGULATIONS FOR DEPOSIT OPERATIONS

M. FEDERAL REGULATORY AGENCIES of Financial Institutions (FI)

- a) **Federal Reserve Board (Board of Governors of the Federal Reserve) (FRB)** Issues regulations, by authority of Congress, implements Federal Reserve Act, and other laws pertaining to a wide range of banking and financial activities. The Regulations are codified at 12 Code of Federal Regulations (12 CFR 201 et seq.) and can be located on the web at <http://federalreserve.gov/regulations>. The Board interpretations, which are labeled "Commentary," follow the sections of each regulation and offer important information and guidance for compliance.
- b) **Office of Thrift Supervision (OTS)** Primary regulator of all federally chartered and many state-chartered thrift institutions, which include savings banks and savings and loan associations. Website: <http://www.ots.treas.gov>.

Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") eliminates the OTS effective one year after enactment of the legislation (subject to a six month extension if determined by the Secretary of the Treasury).but preserves the Thrift charter. All OTS functions, powers, authorities, rights and duties will be transferred to the Federal Reserve, the OCC or the FDIC.
- c) **Office of the Comptroller of the Currency (OCC)** Charters, regulates, and supervises all national banks. It also supervises the federal branches and agencies of foreign banks. Website: <http://www.occ.treas.gov>.
- d) **Federal Deposit Insurance Corporation (FDIC)** An independent agency created by Congress in 1933, the FDIC supervises banks, insures deposits up to – either unlimited for demand deposit accounts or \$250,000 for interest-bearing accounts. Beginning December 31, 2010 through December 31, 2012, deposits held in non-interest bearing transaction accounts will be fully insured, regardless of the amount in the account, at all FDIC-insured accounts will be fully insured, regardless of the amount in the account, at all FDIC-insured institutions. (Note: New Amounts!!) and helps maintain a stable and sound banking system. Website: <http://www.fdic.gov>.
- e) **Federal Trade Commission (FTC)** Consumer protection in trade and marketing Website: <http://www.ftc.gov>.
- f) **Financial Crimes Enforcement Network (FinCEN)** A network of the Department of Treasury that was created to safeguard the financial system from the abuses of financial crime such as terrorist financing, money laundering and other illicit activity, and strives to foster interagency and global cooperation against domestic and international financial crimes, and to provide policies for these purposes. Website: <http://www.fincen.gov>.
- g) **Bureau of Consumer Financial Protection ("CFPB")**. Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") established the Bureau.

The Bureau is within the Federal Reserve System but is independent; charged to "regulate the offering and provision of consumer financial products or services under the Federal consumer laws." The Bureau is charged with creating new regulations and will be the inheritor of the existing consumer regulations. Six primary functions: (1) conducting financial education programs; (2) responding to consumer complaints; (3) collecting, researching, monitoring, and publishing information relevant to the functioning of markets for consumer financial products; (4) identifying risks to consumers and the proper functioning of markets;

(5) supervising covered persons for compliance with federal consumer financial law and taking appropriate enforcement action to address violations; and (6) issuing rules, orders, and guidance implementing federal consumer financial law.

Head of the Bureau will be the director, a presidential appointee that must be confirmed by the Senate, who will serve for a five year term. The director of the Bureau has direct power and does not report to any board of directors. The director is authorized to employ attorneys, compliance examiners, analysts, economists, statisticians, and others as deemed necessary by the director. In addition the Federal Reserve is required to transfer its consumer protection functions to the Bureau. A large number of Federal Reserve employees will migrate to the Bureau.

Checks and balances imposed on the Bureau?

Section 1022 of Dodd Frank requires that the Bureau consult with the appropriate prudential regulators or other federal agencies “regarding consistency of [any proposed rule] with prudential, market, or systemic objectives administered by such agencies.” If the prudential regulator objects, the Bureau must include a description of the objection and the basis for the Bureau’s decision to overrule it.

Section 1023 of Dodd-Frank provides that, upon petition of one of the members of the newly created Financial Stability Oversight Council which is being established to manage systemic risk, the Financial Stability Oversight Council may set aside a final regulation by a two-thirds vote if it finds the rule “would put the safety and soundness of the United States banking system or the stability of the financial system of the United States at risk” Members of the Financial Stability Oversight Council are: Secretary of the Treasury (Chair of the Council); Chair of FRB Board of Governors; Comptroller of the Currency; Director of the Bureau; Chair of the SEC, Chair of the FDIC, Chair of the Futures Trading Commission; Director of the FHFA; Chair of the Board of the NCUA; a presidential appointee with insurance expertise.

The Bureau is required to have specific functional units including: (1) the research unit; (2) the consumer complaint unit; (3) the fair lending unit; (4) the financial education unit; (5) the military service member unit; and (6) the older Americans unit.

Central to its authority is the authority granted under Section 1031 of Dodd-Frank to adopt rules prohibiting unfair, deceptive or abusive acts or practices. There are two definitional guidelines in Dodd-Frank (1) An act or practice is unfair” if there is a reasonable basis for the Bureau to conclude that “the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers” and the “substantial injury” is not outweighed by countervailing benefits; (2) Acts or practices are “abusive” if the act or practice “materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service” or if the act or practice takes unreasonable advantage of a consumer’s lack of understanding of the risks or conditions of the product or service.

The Bureau will have broad supervisory and enforcement authority. The Bureau is authorized to examine and enforce the consumer protection regulations with respect to banks, thrifts, and credit unions with assets more than \$10 billion; all mortgage-related businesses; and “larger participants” as defined by a rule to be made by the Bureau. As to banks, etc. with assets of \$10 billion or less, these institutions will continue to be examined by their prudential regulator but the Bureau may still examine these institutions “on a sampling basis.”

SUMMARY OF DEPOSIT OPERATIONS REGULATIONS

N. Regulation D - Reserve Requirements (12 CFR 204 et seq.)

- a) Regulation D identifies reserve requirements for depositary banks; Defines all accounts
 - i) Demand Deposit, does NOT include NOW Accounts

- ii) Time Deposit (must have an early withdrawal penalty of at least seven days' simple interest on amounts withdrawn within the first six days after deposit)
- iii) Savings Deposit, includes Money Market Deposit Accounts (MMDA)
- b) Transaction limits on Savings Accounts and Money Market Deposit Accounts
 - i) No more than six transfers and withdrawals by means of a preauthorized or automatic transfer or telephonic agreement, order or instruction.
 - ii) Unlimited withdrawals (payments to depositor) when made in person, by mail, messenger, ATM, or telephone.
- c) Right to require 7-day notice prior to withdrawal on Savings Accounts (includes MMDAs),
- d) NOW Account requirements/Who may own a NOW Account (Interest-bearing, unlimited withdrawals by check, or other items, deposit account—with the end of Reg Q, it may be time to eliminate the account type but if you offer it be sure to follow the limitations)
 - i) Individuals, including a sole proprietor using a fictitious name
 - ii) Nonprofit organizations
 - iii) Pension funds, escrow accounts, security deposits and other funds established under agency agreements if the entire beneficial interest is held
 - iv) Governmental units
 - v) Funds held by a fiduciary (including corporate fiduciaries) if all beneficiaries would be eligible for a NOW account

O. Regulation E - Electronic Funds Transfers (12 CFR Part 205)

- a) Purpose - Regulation E implements the Electronic Funds Transfer Act (EFTA), intended to protect consumer rights and safeguards and to define rights and responsibilities for electronic fund transfers (EFTs).
- b) Requirements:
 - i) Disclosures for consumer electronic transactions
 - ii) Rules for determining liabilities and error resolution procedures
 - iii) ATM Fee disclosures
- c) Who/What Does Reg E Cover?
 - i) Consumers with EFTS to deposit accounts plus Payroll Cards
- d) Not covered:
 - i) Business accounts
 - ii) Credit card accounts
 - iii) Loan accounts
- e) What is an EFT? An EFT is defined as "...any transfer of funds that is initiated through an electronic terminal, telephone, computer, or magnetic tape for the purpose of ordering, instructing, or authorizing a financial institution to debit or credit a consumer's account." (205.3)
- f) Examples:
 - i) Debit Card/POS transaction
 - ii) ATM transactions
 - iii) Direct deposits or withdrawals of funds
 - iv) Transfers initiated by telephone

- v) Transfers resulting from debit card transactions, whether or not initiated through an electronic terminal.
- g) What are NOT an EFT?
 - i) Checks , drafts or similar paper instruments, including a check guarantee
 - ii) Wire transfers
 - iii) Automatic transfers – any transfer of funds under an agreement between a consumer and an FI which provides that the FI will initiate individual transfers without a specific request from the consumer.
 - iv) Telephone initiated transfers that are not under a bill payment or other written plan.
 - v) Securities and commodities transfers – any transfer of funds the primary purpose of which is the purchase or sale of a security or commodity.
 - vi) Transfers for small institutions with assets <\$100MM
 - vii) E-checks - ACH transfer (POP, ARC, WEB, TEL) where the consumer provided a check to a merchant (at POS, by phone, via the Internet, or by mail) allowing the merchant to capture the RTN, acct # and serial #, to initiate the transfer.
- h) Disclosure Requirements
 - i) Initial disclosure — Before the first EFT
 - ii) Content:
 - (1) *Liability of consumer.* A summary of the consumer's liability, for unauthorized electronic fund transfers.
 - (2) *Telephone number and address.* The telephone number and address of the person or office to be notified when the consumer believes that an unauthorized electronic fund transfer has been or may be made.
 - (3) *Business days.* The FI's business days.
 - (4) *Types of transfers; limitations.* The type of electronic fund transfers that the consumer may make and any limitations on the frequency and dollar amount of transfers.
 - (5) *Fees.*
 - (6) *Documentation.* A summary of the consumer's right to receipts and periodic statements.
 - (7) *Stop payment.* A summary of the consumer's right to stop payment of a preauthorized electronic fund transfer and the procedure for placing a stop-payment order.
 - iii) Change in terms — At least 21 days before effective date of the change if the change would result in increased fees; increased liability; fewer types of available electronic fund transfers; or stricter limitations on the frequency or dollar amount of transfers.
 - iv) Error resolution notice — At least annually
 - v) Periodic statements —
 - (1) At least monthly if an EFT occurred in the cycle
 - (2) At least quarterly if no EFT occurred
 - vi) Transaction receipts — Must be available from the electronic terminal at the time the consumer initiates the EFT
- i) ATM Fee Disclosures
- j) Error Resolution Procedures

- i) What is an Error?
 - ii) Unauthorized EFT
 - iii) Incorrect EFT
 - iv) Omission of EFT from the periodic statement
 - v) Receipt of incorrect amount of cash from an electronic terminal
 - vi) Consumer's request for documentation regarding an EFT
 - vii) FI must treat the request as notice of an error unless it is clear the consumer is requesting duplicate records, i.e., for tax purposes (205.11)
- k) Notice of Error
- i) May be oral or written
 - (1) If oral, the FI may request written confirmation within 10 business days of the oral notice. Request must be made at the time the oral notice is given.
 - ii) Usually must be made within 60 days of the date the periodic statement was sent.
 - iii) If the notice is a request for documentation, the timeframe is 60 days from the time the documentation is provided.
- l) Investigation
- i) FI shall determine if an error occurred within 10 business days of the notice of error and this includes an oral notice of error. Don't wait for the documentation, which may not come.
 - ii) If the investigation cannot be completed within 10 days, the FI may take up to 45 days from the notice date, provided:
 - (1) Provisional credit is given to the consumer in the amount of the alleged error.
 - (2) FI may decline to issue provisional credit if it properly requested and did not receive written confirmation of an oral notice of error.
 - iii) The 45 day timeframe is extended to 90 days for
 - (1) New accounts (open <30 days before EFT)
 - (2) POS/debit card transactions
 - (3) Transactions not initiated within a state
 - iv) FI may correct the error without investigating
 - v) A review of the FI's own records is satisfactory
 - vi) FI must report the results of the investigation within 3 business days of conclusion
 - vii) If an error is located:
 - (1) Must correct within 1 business day
 - (2) Must refund any fees charged due to the error
 - (3) Must make interest adjustments for interest bearing accounts
 - viii) If no error is located:
 - (1) Explanation of investigation must be in writing
 - (2) If provisional credit was given, cannot simply cancel provisional credit. Must honor checks/debits for five business days after notification.
- m) Consumer Liability
- i) Applies only to unauthorized EFTS

- ii) \$50 if the consumer notifies the FI within 2 business days of learning of the loss or theft of an access device
 - iii) \$500 if the consumer fails to notify the FI within 2 business days AND the FI can show the EFTs would not have occurred if timely notice was given
 - iv) Unlimited for unauthorized EFTs occurring more than 60 days prior to the error notice
 - v) Extenuating circumstances may require the FI to extend the 60 day timeframe to a reasonable period
- n) Common Compliance Pitfalls
- i) Following payment system rules vs. Reg E (but you may be obligated to give full credit and not charge the consumer for his/her share)
 - ii) ACH
 - iii) Visa/MC
 - iv) Time limits (business vs. calendar days)
 - v) Delaying investigation while waiting for written correspondence from consumer
 - vi) Refusing to investigate because of 60 day timeframe (check with local counsel)
 - vii) Not recognizing a request for documentation as a notice of error
- o) Section 205.17 on Overdraft Services
- i) Definitions “Overdraft service” is a service under which a financial institution assesses a fee or charge on a consumer’s account held by the institution for paying a transaction (including a check or other item) when the consumer has insufficient or unavailable funds in the account.” Does not include lines of credit subject to Regulation Z or a service that transfers funds from another deposit account; or line of credit or transaction exempt from Regulation Z.
 - ii) Opt-in requirement. FI may not assess a fee or charge on a consumer’s account for paying an ATM or one-time debit card transaction pursuant to the FI’s overdraft service unless (a) the FI provides the consumer with a notice in writing (or electronically if the consumer consents) describing the FI’s overdraft service; (b) provides a reasonable opportunity for the consumer to opt-in or affirmatively consent to the service for ATM or one-time debit card transactions; (c) obtains the consumer’s opt-in; and (d) provides the consumer with a written confirmation of the opt-in, such consent may be electronic if the consumer has consented.
 - iii) Note Model Form A-9
- Caution: While Examiners are reviewing for “technical compliance”, they are also looking at whether the program has aspects which could be characterized as unfair or deceptive.
- p) **205.18 Requirements for financial institutions offering payroll card accounts.**
- (a) *Coverage.* FIs must comply with all applicable requirements of the EFTA and this part with respect to payroll card accounts except as provided in this section.
 - (b) *Alternative to periodic statements.* (1) FI need not furnish periodic statements required by §205.9(b) if the institution makes available to the consumer –
 - (i) The consumer’s account balance, though a readily available telephone line;
 - (ii) An electronic history of the consumer’s account transactions, such as through an Internet Web site, that covers at least 60 days preceding the date the consumer electronically accesses the account; and
 - (iii) A written history of the consumer’s account transactions that is provided promptly in response to an oral or written request and that covers at least 60 days preceding the date the FI receives the consumer’s request.

(2) The history of account transactions provides information under paragraphs (b)(1)(ii) of this section.

(c) *Modified requirements.* FIs that provides information under paragraph (b) of this section, shall comply with the following:

(1) *Initial disclosures.* FI must modify the disclosures under §205.7(b) by disclosing –

(i) *Account information.* A telephone number the consumer may call to obtain the account balance, the means by which the consumer can obtain an electronic account history, such as the address of an Internet Web site, and a summary of the consumer's right to receive a written account history upon request (in place of the summary of the right to receive a periodic statement required by §205.7(b)(6), including a telephone number to call to request a history.

(ii) *Error resolution.* A notice concerning error resolution.

(2) *Annual error resolution notice.* FI shall provide an annual notice concerning error resolution. Alternatively, FI may include on or with each electronic and written history a notice substantially similar to the abbreviated notice for periodic statements.

(3) *Limitations on liability.* (i) For purposes of §205.6(b)(3), the 60-day period for reporting any unauthorized transfer shall begin on the earlier of:

(A) The date the consumer electronically accesses the consumer's account provided that the electronic history made available to the consumer reflects the transfer; or

(B) The date the FI sends a written history of the consumer's account transactions requested by the consumer.

(4) *Error resolution.* (i) FI must comply with requirements of 205.11 in response to an oral or written notice of an error from the consumer that is received but the earlier of -

(A) The date the consumer electronically accesses the consumer's account provided that the electronic history made available to the consumer reflects the transfer; or

(B) Sixty days after the date the FI sends a written history of the consumer's account transactions requested by the in which the alleged error is first reflected.

(ii) In lieu of following the procedures in paragraph ©(4)(i) of this section, FI complies with the requirements for resolving errors in §205.11 if it investigates any oral or written notice of an error from the consumer that is received by the institution within 120 days after the transfer allegedly in error was credited or debited to the consumer's account.

[Reg. E, 71 FR 51449, Aug. 30, 2006]

q) **§205.20 Requirements for gift cards and gift certificates.**

(a) *Definitions:*

(1) *Gift certificate* means a card, code, or other device that is:

(i) Issued on a prepaid basis primarily for personal, family, or household purposes to a consumer in a specified amount that may not be increased or reloaded in exchange for payment; and

(ii) Redeemable upon presentation at a single merchant or an affiliated group of merchants for goods or services.

(2) *Store gift card* means a card, code, or other device that is:

(i) Issued on a prepaid basis primarily for personal, family, or household purposes to a consumer in a specified amount that may not be increased or reloaded in exchange for payment; and

(ii) Redeemable upon presentation at a single merchant or an affiliated group of merchants for goods or services.

- (3) *General-use prepaid card* means a card, code, or other device that is:
- (i) Issued on a prepaid basis primarily for personal, family, or household purposes to a consumer in a specified amount that may not be increased or reloaded in exchange for payment; and
 - (ii) Redeemable upon presentation at a single merchant or an affiliated group of merchants for goods or services.
- (4) *Loyalty, award, or promotional gift card* means a card, code, or other device that is:
- (i) Is issued on a prepaid basis primarily for personal, family, or household purposes to a consumer in connection with a loyalty, award, or promotional program;
 - (ii) Redeemable upon presentation at one or more merchants for goods or services, or usable at automated teller machines; and
 - (iii) Sets forth the following disclosures, as applicable:
 - (A) A statement indicating that the card, code, or other device is issued for loyalty, award, or promotional purposes, which must be included on the front of the card, code, or other device;
 - (B) The expiration date from the underlying funds, which must be included on the front of the card, code, or other device;
 - (C) The amount of any fees that may be imposed in connection with the card, code, or other device, and the conditions under which they may be imposed, which must be provided on or with the card, code, or other device; and
 - (D) A toll-free telephone number and, if one is maintained, a Web site, that a consumer may use to obtain fee information, which must be included on the card, code, or other device.
- (5) *Dormancy or inactivity fee*. The terms “dormancy fee” and “inactivity fee” mean a fee for non-use of or inactivity on a gift certificate, store gift card, or general-use prepaid card.
- (6) *Service fee*. means a periodic fee for holding or use of a gift certificate, store gift card, or general-use prepaid card. A periodic fee includes any fee that may be imposed on a gift certificate, store gift card, or general-use prepaid card from time to time for holding or using the certificate or card.
- (7) *Activity*. means any action that results in an increase or decrease of the funds underlying a certificate card, other than the imposition of a fee, or an adjustment due to an error or a reversal of a prior transaction.
- (b) *Exclusions*. The terms “gift certificate,” “store gift card,” and “general-use pre-paid card” do not include any card, code, or other device that is:
- (1) Useable solely for telephone services;
 - (2) Reloadable and not marketed or labeled as a gift card or gift certificate. The term “reloadable” includes a temporary non-reloadable card issued solely in connection with a reloadable card, code, or other device;
 - (3) A loyalty, award, or promotional gift card;
 - (4) Not marketed to the general public;
 - (5) Issued in paper form only; or
 - (6) Redeemable solely for admission to events or venues at a particular location or group of affiliated locations, or to obtain goods or services in conjunction with admission to such events or venues, at the event or venue or at specific locations affiliated with and in geographic proximity to the event or venue.
- (c) *Form of disclosures* -
- (1) Clear and conspicuous..

(2) *Format.* Disclosures made under this section generally must be provided to the consumer in written or electronic form and generally must be in a retainable form. Disclosures provided under paragraphs (c)(3) and (h)(2) of may be given orally.

(3) *Disclosures prior to purchase.* Before a gift certificate, store gift card, or general-use prepaid card is purchased, a person that issues or sells such certificate or card must disclose to the consumer the information required by paragraphs (d)(2), (e)(3), and (f)(1). The fees and terms and conditions of expiration that are required to be disclosed prior to purchase may not be changed after purchase.

(4) *Disclosures on the certificate card.* Disclosures required by paragraphs (a)(4)(iii), (d)(2), (e)(3), and (f)(2) of this section **must be made on the certificate or card, or in the case of a loyalty, award, or promotional gift card, on the card, code, or other device.** A disclosure made in an accompanying terms and conditions document, on packaging surrounding a certificate or card, or on a sticker or other label affixed to the certificate or card does not constitute a disclosure on the certificate or card. For an electronic certificate or card, disclosures must be provided electronically on the certificate or card provided to the consumer. An issuer that provides a code or confirmation to a consumer orally must provide to the consumer a written or electronic copy of the code or confirmation promptly, and the application disclosures must be provided on the written copy of the code or confirmation.

(d) *Prohibition on imposition of fees or charges.* No person may impose a dormancy, inactivity, or service fee with respect to a gift certificate, store gift card, or general-use prepaid card, unless:

- (1) There has been no activity with the respect to the certificate or card, in the one-year period ending on the date on which the fee is imposed;
- (2) The following are stated, as applicable, clearly and conspicuously on the gift certificate, store gift card, or general-use prepaid card:
 - (i) The amount of any dormancy, inactivity, or service fee that may be charged;
 - (ii) How often such fee may be assessed; and
 - (iii) That such fee may be assessed for inactivity; and
- (3) Not more than one dormancy, inactivity, or service fee is imposed in any given calendar month.

(e) *Prohibition on sale of gift certificates or cards with expiration dates.* No person may sell or issue a gift certificate, store gift card, or general-use prepaid card with an expiration date, unless:

- (1) The person has established policies and procedures to provide consumers with a reasonable opportunity to purchase a certificate or card with at least five years remaining until the certificate or card expiration date;
- (2) The expiration date for the underlying funds is at least the later of:
 - (i) Five years after the date the gift certificate was initially issued, or the date on which funds were last loaded to a store gift card or general-use prepaid card; or
 - (ii) The certificate or card expiration date, if any;
- (3) The following disclosures are provided on the certificate or card, as applicable:
 - (i) The expiration date for the underlying funds or, if the underlying funds do not expire, that fact;
 - (ii) A toll-free number and, if one is maintained, a Web site that a consumer may use to obtain a replacement certificate or card after the certificate or card expires if the underlying funds may be available; and
 - (iii) Except where a non-reloadable certificate or card bears an expiration date that is at least seven years from the date of manufacture, a statement, disclosed with equal prominence and in close proximity to the certificate or card expiration date, that:

- (A) The certificate or card expires, but the underlying funds either do not expire or expire later than the certificate or card, and;
- (B) The consumer may contact the issuer for a replacement card; and
- (4) No fee or charge is imposed on the cardholder for replacing the gift certificate, store gift card, or general-use prepaid card or for providing the certificate or card holder with the remaining balance in some other manner prior to the funds expiration date, unless such certificate or card has been lost or stolen.

(f) *Additional disclosure requirements for gift certificates or cards.* The following disclosures must be provided in connection with a gift certificate, store gift card, or general-use prepaid card, as applicable:

(1) *Fee disclosures.* For each type of fee that may be imposed in connection with the certificate or card (other than a dormancy, inactivity, or service fee subject to the disclosure requirements under paragraph (d)(2) of this section), the following information must be provided on or with the certificate or card:

- (i) The type of fee;
- (ii) The amount of the fee (or an explanation of how the fee will be determined); and
- (iii) The conditions under which the fee may be imposed.

(2) *Telephone number for fee information.* A toll-free telephone number and, if one is maintained, a Web site, that a consumer may use to obtain information about fees described in paragraphs (d)(2) and (f)(1) of this section must be disclosed on the certificate or card.

(g) *Compliance dates.* - (1) *Effective date for gift certificates, store gift cards, and general-use prepaid gift cards.* Except as provided in paragraph (h), the requirements of this section apply to any gift certificate, store gift card, or general-use prepaid card sold to a consumer on or after August 22, 2010, or provided to a consumer as a replacement for such certificate or card.

(2) *Effective date for loyalty, award, or promotional gift cards.* The requirements in paragraph (a)(4)(iii) apply to any card, code, or other device provided to a consumer in connection with a loyalty, award, or promotional program if the period of eligibility for such program began on or after August 22, 2010.

(h) *Temporary exemption – (1) Delayed effective date.* For any gift certificate, store gift card, or general-use prepaid card produced prior to April 1, 2010, the effective date of the requirements of paragraphs (c)(3), (d)(2), (e)(1), (e)(3), and (f) of this section is January 31, 2011, provided that an issuer of such certificate or card:

- (i) Complies with all other provisions of this section;
- (ii) Does not impose an expiration date with respect to the funds underlying such certificate or card;
- (iii) At the consumer's request, replaces such certificate or card if it has funds remaining at no cost to the consumer; and
- (iv) Satisfies the requirements of paragraph (h)(2) of this section.

(2) *Additional disclosures.* Issuers relying on the delayed effective date in §205.20(h)(1) must disclose through in-store signage, messages during customer service calls, Web sites, and general advertising, that:

- (i) The underlying funds of such certificate or card do not expire;
- (ii) Consumers holding such certificate or card have a right to a free replacement certificate or card, accompanied by the packaging and materials typically associated with such certificate or card; and

(iii) Any dormancy, inactivity, or service fee for such certificate or card that might otherwise be charged will not be charged if such fees do not comply with Section 915 of the Electronic Fund Transfer Act.

(3) *Expiration of additional disclosure requirements.* The disclosures in paragraph (h)(2) of this section:

(i) Are not required to be provided on or after January 31, 2011, with respect to in-store signage and general advertising.

(ii) Are not required to be provided on or after January 31, 2013, with respect to messages during customer service calls and Web sites.

[Reg. E, 75 FR 16614, Apr. 1, 2010, as amended at 75 FR 50687, Aug. 17, 2010]

P. Regulation CC – Check Collection and Expedited Funds Availability (12 CFR 229)

- a) The Federal Reserve Board issued Regulation CC to implement the Funds Availability Act. Regulation CC governs the availability of funds deposited in checking accounts and the collection and return of checks. Regulation CC is divided into four subparts:
- i) Subpart A: Definitions and enforcement authority
 - ii) Subpart B: The schedules within which banks must make funds available for withdrawal, exceptions to the schedules, disclosure of funds availability policies, and payment of interest
 - iii) Subpart C: Governs the collection and return of checks
 - iv) Subpart D: Rules re: Substitute Checks (implementation of the Check Clearing for the 21st Century Act or Check 21 Act)

Q. Check 21 Act and Subpart D of Regulation CC Impacts check presentment and payment process, including warranties and indemnities associated with processing substitute checks (below).

Regulation J -- Collection of Checks and Other Items (12 CFR 210) Regulation J also governs the collection of checks and other cash and non-cash items and the handling of returned checks by Federal Reserve Banks.

- a) Each Reserve Bank is to receive and handle items in accordance with Regulation J, and to issue operating circulars governing the details of its handling of items and other matters deemed appropriate by the Reserve Bank.
- b) Regulation J, subpart C of Regulation CC, and the Operating Circulars of the Reserve Banks are binding on all parties interested in an item handled by any Reserve Bank.

R. Conflict Between Regulations CC and J and State Law

- a) The Uniform Commercial Code, as enacted in each state, is the state law which governs bank collections and deposits.
- b) Article 3: Negotiable instruments, checks
- c) Article 4: Collection of checks through the banking system, sets forth time requirements for payments of check, and the respective liabilities of the banks in the check collection process
- d) If there is conflict between a provision of Articles 3 and 4 of the Commercial Code, and any of the federal rules, either Regulation CC or regulation J, Operating Circulars, or clearinghouse rules, the latter govern over Commercial Code (Federal law preempts State law).

S. **Regulation CC - Check Availability and Collection [**

- a) Purpose
 - i) Obligates financial institutions to make funds deposited into accounts available for withdrawal within a specific time period
 - ii) Expedites check processing, including returns
 - iii) Consumer protection in the deposit and check collection process

- b) Some Basics
 - i) Accounts (consumer & business) Accounts that allow “unlimited third party transfers?”
 - ii) What types of payments and credits are subject to Regulation CC? For example, “electronic payments” - a wire transfer or ACH credit transfer-are included; however, “electronic payment” does *not* include ACH debit transfer
 - iii) Business Day — calendar day other than Sat./Sun. and specified holidays
 - iv) Banking Day — part of any business day on which Bank is open. Cut-off for type of deposit will determine banking day of deposit
 - v) Next Day/2nd Day Items
 - vi) Local/Non Local/Intra-California checks*
 - vii) Proprietary/Non-Proprietary ATMs
 - viii) Foreign Banks

***IMPORTANT NOTE: Due to consolidation of the Federal Reserve’s Check Processing Centers, all checks drawn on banks within the United States are now considered Local Checks. Non-Local checks no longer exist in practice.**

- c) Calculating Availability
 - i) The regulation does not have a “Same Day” requirement (other rules may apply)
 - ii) Next Day items:
 - (1) Cash (in-person to a bank employee)
 - (2) Electronic payments (may be superseded by NACHA rules of same day)
 - (3) U.S. Treasury checks (deposited in person to a bank employee in the payee’s acct)
 - (4) USPS money orders, FRB & FHLB checks (deposited in person to a bank employee in the payee’s acct)
 - (5) Cashier’s checks and State or local government checks (deposited in person to a bank employee in the payee’s account, with a special deposit slip or deposit envelope if required by bank)
 - (6) On-U.s checks (same processing region)
 - (7) Lesser of \$100 or the aggregate amount deposited on any one banking day.
 - iii) 2-Day Items (Second business day after the banking day of deposit)
 - (1) local check
 - (2) U.S. Treasury checks, USPS money orders, FRB & FHLB checks, cashier’s checks and state or local government checks not otherwise treated as Next Day Items.

- iv) 5-Day (Fifth business day after the banking day of deposit)
 - (1) Non-local checks
 - (a) NOTE – 4-day intra-CA rule under CA Regulation became moot with the consolidation of the LA Fed Check Processing hub into San Francisco – causing deposited checks drawn on CA accounts to be treated as local checks.
 - v) \$400 Rule allows FI to delay, by one day, the customer's ability to withdraw in cash a portion of a deposit of local and/or non-local checks
- d) Types of Holds
- i) Case-by-case holds
 - (1) Local — maximum 2 days
 - (2) Non-Local — maximum 5 days
 - (3) \$100 of total deposit available next day
 - ii) Exception holds
 - (1) Local — maximum 7 days
 - (2) Non-Local — maximum 11 days
 - (3) Intra-California — maximum 10 days
 - (4) \$100 availability not always required
 - iii) Exception Hold Types
 - (1) New Accounts (first 30 days)
 - (2) Large Deposits (>\$5,000)
 - (3) Re-Deposited Returned Items
 - (4) Repeated Overdrafts
 - (5) Emergency Conditions
 - (6) Reasonable Cause to Doubt Collectibility
 - iv) Written notice to depositors when Case-by-Case or Exception Hold exercised
 - (1) Customer's account
 - (2) Date of the deposit
 - (3) Amount of the deposit
 - (4) Reason the exception hold was invoked, and
 - (5) Time period within which the funds will be available for withdrawal.
 - (6) Notice given at the time of deposit for teller deposits, or no later than the first business day following the day the facts became known.
 - (a) If Exception Hold is invoked backshop, the bank shall not assess any fees for any subsequent overdrafts or return checks resulting from the hold and the check is ultimately paid by the paying bank.
 - v) Required Expedited Returns
 - (1) Day 1: Item presented to Paying Bank
 - (2) Day 2: If not paying item. Paying Bank must return by Midnight (Reg J/UCC) or must return utilizing the two-day/four-day test for forward collection test.
 - (3) Day 3: Large Item Return Notification for items being returned over \$2,500 must be at the Institution of First Deposit (IFD) by 4:00 p.m. (If

receiving such a notice, it is an opportunity to use a “doubtful collectibility” exception hold.)

- vi) Disclosure of Availability Schedule
 - (1) In writing
 - (2) Clear and conspicuous
 - (3) Capable of retention
 - (4) Grouped together/separated from other information
 - (5) One joint holder/for one account if applicable to accounts
 - (6) OK to have different schedules for different accounts
 - (7) Not required if dormant or inactive account
- vii) General Notes about Regulation CC
 - (1) Reg CC sets the parameters for availability and processing timeliness your bank policy can be anywhere within these parameters.
 - (2) Reg CC does not mandate holds or require you to accept a check.
 - (3) Avoid Compliance Pitfalls
 - (a) Train employees
 - (b) Test automated/system hold placements
 - (c) Monitor multiple holds
 - (d) Monitor \$100 availability
 - (e) Manage hold placement based on “models”
 - (f) Notices must match actuality
 - (4) Updates to Reg CC / Fed check processing sites
 - (5) Check Truncation —vs.- Check Conversion
 - (6) Substitute Check rules apply to all types of accounts
 - (7) Substitute Check rules do not affect availability schedule of Regulation CC.

Important Change: Dodd-Frank Section 1086 changes Act – increases the \$100 to \$200 and provides for inflation increases.

Expedited Funds Availability Improvements- Section 603 of the Expedited Funds Availability Act ([12 U.S.C. 4002](#)) is amended--

(1) In subsection (a)(2)(D), by striking ‘\$100’ and inserting ‘\$200’; and

(2) In subsection (b)(3)(C), in the subparagraph heading, by striking ‘\$100’ and inserting ‘\$200’; and

(3) In subsection (c)(1)(B)(iii), in the clause heading, by striking ‘\$100’ and inserting ‘\$200’.

(f) Regular Adjustments for Inflation- Section 607 of the Expedited Funds Availability Act ([12 U.S.C. 4006](#)) is amended by adding at the end the following:

‘(f) Adjustments to Dollar Amounts for Inflation- The dollar amounts under this title shall be adjusted every 5 years after December 31, 2011, by the annual percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers,

as published by the Bureau of Labor Statistics, rounded to the nearest multiple of \$25.

T. Substitute Checks — Check 21 and Subpart D of Regulation CC

- a) A “Substitute Check” is
 - i) The equivalent of an original check for all persons and purposes, including any provision of federal or state law, if the substitute check:
 - ii) “accurately represents all of the information on the front and back of the original check” (including all endorsements) at time of truncation, and
 - iii) Bears the legend, “This is a legal copy of your check. You can use it the same way you would use the original check.”
 - iv) The Reconverting bank shall identify itself as such on any substitute check, so as to preserve previous reconverting bank identifications.
- b) General Provision and Substitute Check Warranties:
 - i) Generally, a substitute check can be used at any point in the collection system, without agreement by the recipient, so long as each user bank that receives consideration for it warrants (as a matter of law) that:
 - ii) It meets requirements for “legal equivalence”, namely:
 - (1) “Accurately represents all of the information on the front and back of the original check” (including all endorsements) at time of truncation, and
 - (2) Bears the legend: This is a legal copy of your check. You can use it the same way you would use the original check.” and,
 - iii) No one will be asked to make a payment on a check that they have already paid.
 - iv) Reconverting bank shall identify itself as such on any substitute check, so as to preserve previous reconverting bank identifications.
- c) Indemnity
 - i) Generally, a reconverting bank and all other banks that handle a substitute check and receive consideration for it shall indemnify for losses (see amount below) incurred by any recipient of the substitute check due to the receipt of a substitute check instead of the original check.
 - (1) If Sec. 5 §5004 (breach of warranty — any loss, including costs and reasonable attorney's fees proximately caused by the breach.
 - (2) If no Sec. 5 §50041 breach — up to amount of check, plus interest and expenses (including costs and reasonable attorney's fees.)
 - ii) Comparative negligence if loss due in whole or in part from the negligence or failure to act in good faith on the part of an indemnified party.
 - iii) Production of original check or accurate copy will limit losses to those covered by the indemnity that are incurred before it is provided, but will not absolve the bank from any liability on a warranty.
 - iv) Indemnified party must cooperate.
- d) Expedited Recredit for Consumers
 - i) Consumer can make claim for expedited recredit from his/her bank if he/she asserts in good faith that bank charged account for a substituted check, and
 - ii) Check not properly charged, or Consumer has warranty claim regarding it, and
 - iii) Loss incurred, and

- iv) An original check or better copy is necessary to determine validity of the claim (see (i) above).
 - v) 40-day period, after statement mailed or substitute check made available, to make claim. Reasonable extensions allowed for extenuating circumstances.
 - vi) Procedure for making claim must be followed.
 - vii) Recredit due if bank has not
 - viii) provided original or copy of check, and
 - ix) demonstrated that the substitute check was properly charged to the account.
 - x) Must recredit within one business day of determining validity of claim.
 - xi) Pending investigation, must recredit up to \$2500 by 10th business day, and the remaining, if any, by the 45th calendar day, BUT
 - xii) May delay availability of recredited funds pending investigation if new account, repeated overdrafts, suspected fraud.
 - xiii) Notices to consumer are required.
 - xiv) Recredit does not absolve the bank from further liability under any other law, e.g. wrongful dishonor.
- e) Expedited Recredit for Banks
- i) 120-day period (after transaction giving rise to the claim) for bank to make claim against an indemnifying bank (Sec. 6 §5005) based on:
 - ii) bank receiving, or paying, a consumer claim (Sec. 7 §5006), and
 - (1) original check, another substitute check, or a better copy is necessary to determine validity of charge to customer account.
 - iii) 10 business days to
 - (1) provide original or copy of check, and
 - (2) recredit claimant bank, or
 - (3) provide information as to why not obligated.
 - iv) Delays in an Emergency
 - (1) Will be excused IF
 - (2) Circumstances beyond the control of a bank, and
 - (3) Bank uses such diligence as the circumstances require.
 - v) Measure of Damages - Except as provided in Indemnity section, any person who, in connection with a substitute check, breaches any warranty of the Act, fails to comply with it or regulations prescribed pursuant to it, shall be liable for lesser of the amount of loss or the amount of the substitute check, and interest and expenses.
 - (1) Comparative negligence applies.
 - vi) Statute of Limitations
 - (1) One year from when cause of action accrues
 - (2) Accrues on date when injured party first learns, or reasonably should have learned, of facts giving rise to the cause of action.
 - (3) Persons, other than Consumers claiming under Sec. 7/§5006, must notify warranting or indemnifying bank within 30 days after the person has reason to know of the claim and the identity of the indemnifying or warranting bank, or such bank is discharged to the extent of any loss caused by the delay in giving notice.

- vii) Consumer Awareness
 - (1) Required notices
 - (a) Content of notice
 - (b) To existing and new customers, and to those who request check copy and get a substitute check
 - (c) Optional model language, safe harbor
 - (2) Effect on Other Law - The Act supersedes any provision of Federal or State law, including the UCC, which is inconsistent with this Act, but only to the extent of the inconsistency.
- viii) Variation by Agreement - Except for Sec. 8 §5007 (recredit procedures for banks), no provision of the Act can be varied by agreement of any person or persons.

Regulation DD — Truth in Savings (12 CFR 230)

Regulation DD is the implementing regulation for Truth In Savings Act (TISA).

- f) Purpose - To promote competition among depository institutions by enhancing the ability of consumers to make informed comparisons and decisions regarding the terms of deposit accounts.
- g) Requirements - Uniform disclosure of the terms and conditions for the payment of interest and the charging of fees in connection with such accounts, for the purpose of allowing consumers to make meaningful comparisons between the competing claims of depository institutions.
- h) Who/What Does Reg DD Cover?
 - ix) Deposit Accounts held by or offered to consumers primarily for personal, family or household purposes
 - x) Includes non-interest bearing consumer accounts
 - xi) IRA and Keogh Accounts
 - xii) Custodial accounts for consumers
 - xiii) What Accounts Are Not Covered by Reg DD
 - xiv) Business Purpose Accounts
 - xv) Custodial and Trust Accounts, if acting in a professional capacity
 - xvi) Attorney-client Trust Accounts
 - xvii) Landlord-tenant security deposit accounts
 - xviii) Mortgage escrow account
 - xix) Accounts held by nonresident aliens/accounts held outside U.S.
- f) Required Reg DD Disclosures
 - i) Account Disclosures
 - (1) Must be provided to a consumer before an account is opened or service is provided.
 - (2) If consumer is not present when the account is opened, the bank shall mail or deliver the disclosures no later than 10 business days after the earlier of the opening of the account or providing of service
 - (a) Consumers opening accounts using electronic communication (email, Internet) must be provided with disclosures before the account is opened or service is provided

- (b) Consider E-Sign Act to effect electronic delivery of disclosures.
- (3) If the account is held by more than one consumer, disclosure may be made to one of the consumers
- (4) Must be provided to consumer upon request
- (5) Can be stated as rate within most recent 7-day period with identification of date: provide telephone number to call to obtain current rate
- (6) Can state the maturity of a time account as a term rather than a date
- (7) Content of Account Disclosures (as applicable):
 - (a) Rate information
 - (b) Compounding and crediting
 - (c) Balance information
 - (d) Fees
 - (e) Transaction limitations
 - (f) Features of time accounts
 - (g) Bonuses
- (8) Subsequent change in terms
- ii) Subsequent Change in Terms
 - (1) Notice is required if change adversely affects any of the above listed items requires
 - (2) change will reduce yield or adversely affect holder of account
 - (3) To all account holders who may be affected
 - (4) Written description of the change
 - (5) By mail, at least thirty (30) calendar days before the change takes effect
 - (6) Notice not required for:
 - (a) Changes in the simple interest rate and APY for variable rate accounts
 - (b) Changes in check printing fees charged by third parties
 - (c) Changes in the terms of a time account with a maturity of one month or less
 - (d) For time accounts, special notice requirements
- iii) Periodic Statements
 - (1) "Periodic Statement" - Any Statement setting forth information about an account that is provided to a consumer on a regular basis four or more times a year.
 - (2) Content of Periodic Statement Disclosure.
- iv) Correction of Disclosure Error
 - (1) Correction of Error - If the Bank discovers an error, it will notify the customer of the error and will correct that error within 60 days.
 - (2) If an error occurs, Reg DD states rules that will determine Bank liability
- v) Calculation of Interest
 - (1) Calculation – Interest must be calculated on the full amount of principal in the account for each day

- (2) Balance computation method —The Bank shall use the same method to determine any minimum balance required to earn interest as it uses to determine the balance on which interest is calculated.
- (3) The Bank may use an additional method which is unequivocally beneficial to the consumer.
- (4) Compounding and crediting — Regulation DD does not require the Bank to compound or credit interest at any particular frequency
- (5) Date interest begins to accrue — Interest shall begin to accrue not later than the business day specified for interest-bearing accounts under Regulation CC. Interest shall begin to accrue until the day funds are withdrawn
- (6) APY Calculation — Formulas stated in Reg DD Appendix.

vi) Advertisement Disclosures

- (1) Advertisements - A “commercial message, appearing in any medium that promotes directly or indirectly the availability of, or a deposit in, an account.”
- (2) Commentary: Includes “commercial messages in visual, oral or print media.
- (3) Covered: Telephone solicitations, ATM screen messages, marketing materials included in account documents, computer screens in lobby, radio ads, newspaper ads, promotional flier.
- (4) Not covered: In-person discussions with consumers about terms for a specific account, information given to consumer about an existing account.
- (5) An advertisement cannot contain misleading or inaccurate information
 - (a) “Free” or “no cost”
 - (b) Interest cannot be referred to as “profit”
 - (c) Conform to Deposit Contract
- (6) An advertisement must contain disclosures required by Regulation DD
- (7) Regulation DD Commentary (amendment): Use of “Free” in marketing - “An advertisement would be deemed to be misleading if the account is described as “free” and the advertisement also promotes account related services for which there is a fee, unless the advertisement clearly and conspicuously indicates that there is a cost associated with the advertised service.”
- (8) APY - Trigger Term
 - (a) Variable rates: statement that rates may change after account is opened
 - (b) Time APY is offered
 - (c) Minimum balance to obtain rate
 - (d) Minimum opening deposit to obtain rate
 - (e) Statement that fees could reduced earnings
- (9) Time Account – Trigger Term
 - (a) Term of the time account
 - (b) Early withdrawal penalties may or will be imposed
 - (c) Required interest payouts, if any.
- (10) Bonus – Trigger Term
 - (a) Annual percentage yield

- (b) Time requirement to obtain the bonus
 - (c) Minimum balance required to obtain the bonus
 - (d) Minimum balance required to open the account, if greater than the minimum to obtain the bonus
 - (e) When the Bonus will be provided.
- (11) Disclosures under 230.11 regarding additional disclosures for overdraft services.
- Effective as of January 1, 2010, all institutions were required to include on periodic statements (i) The total dollar amount for all fees or charges imposed on the account for paying checks or other items when there are insufficient or unavailable funds and the account becomes overdrawn; and (ii) The total dollar amount for all fees or charges imposed on the account for returning items unpaid.
- (12) Disclosures under 230.11 regarding any advertisement promoting the payment of overdrafts
- (a) FI's that advertise the payment of overdrafts must disclose in a clear and conspicuous manner:
- The fee or fees for the payment of each overdraft;
 - The categories of transactions for which a fee for paying an overdraft may be imposed;
 - The time period by which the consumer must repay or cover any overdraft; and
 - The circumstances under which the institution will not pay an overdraft.
- (b) The following are not advertisements:
- An advertisement promoting a service where the FI's payment of overdrafts will be agreed upon in writing and subject to the Board's Regulation Z (12 CFR part 226);
 - A communication by an FI about the payment of overdrafts in response to a consumer-initiated inquiry about deposit accounts or overdrafts. [Providing information about the payment of overdrafts in response to a balance inquiry made through an automated system, such as a telephone response machine, ATM, or an institution's Internet site, is not a response to a consumer-initiated inquiry for purposes of this exception;
 - An advertisement made through broadcast or electronic media, such as television or radio;
 - An advertisement made on outdoor media, such as billboards;
 - An ATM receipt;
 - An in-person discussion with a consumer;
 - Disclosures required by federal or other applicable law;
 - Information included on a periodic statement or a notice informing a consumer about a specific overdrawn item or the amount the account is overdrawn;
 - A term in a deposit account agreement discussing the institution's right to pay overdrafts;

- A notice provided to a consumer, such as at an ATM, that completing a requested transaction may trigger a fee for overdrawing an account, or a general notice that items overdrawing an account may trigger a fee;
- Informational or educational materials concerning the payment of overdrafts if the materials do not specifically describe the institution's overdraft service; or
- An opt-out or opt-in notice regarding the institution's payment of overdrafts or provision of discretionary overdraft services.

(c) See commentary for model language.

U. Joint Agency Overdraft Guidelines

- a) Jointly issued by FDIC, OCC, Federal Reserve Board and NCUA
- b) Guidelines issued to address concern over marketing of overdraft protection programs. Does it encourage consumers to overdraft accounts?
- c) What is an “overdraft program?”
- d) Excludes overdrafts paid on discretionary basis as an accommodation if not promoted
- e) Seven characteristics listed (some or all?):
 - i) Promoted as a service
 - ii) Automatic coverage for accounts that meet certain characteristics
 - iii) Overdraft limit is set
 - iv) Payment by bank is discretionary
 - v) Service may extend to transactions other than checks
 - vi) Flat fee is charged
 - vii) Offering closed-end loans to consumers to repay balances
- f) What is “promotion?”
- g) Disclosure of “aggregate dollar limit”
- h) No Regulation Z coverage for discretionary overdrafts
- i) Regulation B may apply if administered in discriminatory manner (pricing, customer)
- j) Safety and soundness considerations apply to all overdraft programs
 - i) Must adopt formal policies and procedures on all aspects of overdraft activities (including eligibility, dollar limits, repayment plans, suspensions and write-offs)
 - ii) Must treat overdrafts as loans for purposes of regulatory reporting and capital standards
- k) “Best Practices” Listed
 - i) Must not market in a way that encourages intentional overdrafts
 - ii) Must not market in a way that encourages account mismanagement
 - iii) Present as a service to cover inadvertent overdrafts only
 - iv) Inform of all overdraft services if promoting one type of product
 - v) Disclose right not to pay overdraft
 - vi) Disclose dollar amount of overdraft fee, any interest charged, and that more than one fee may apply
 - vii) Do not promote in same advertisement as marketing “free” accounts

- viii) Explanation that transactions may be processed in any order
- ix) Bank's policies may affect amount of fees
- x) Not permitted to adjust clearing policies to inflate fees (OTS)
- xi) Right to opt-out of overdraft protection (opt-in) and clear consumer disclosure
- xii) Notices should be delivered the same day as occurrence

The USA PATRIOT ACT and the International Money Laundering Abatement and Anti-Terrorist Financing Act

- l) Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT ACT) Act of 2001
- m) Standards for Verification of Customer Information at Account Opening (Customer Identification Program)
- n) Customer Identification Program (CIP)
 - i) Requires the FI to establish a written program for the identification and verification of the customer at account opening
 - ii) Record keeping requirements for the information used to identify and verify the customer
 - iii) Requires procedures for determining whether the person appears on any list of known or suspected terrorists or terrorist organizations
- o) Information Security and Risk Assessment Program - Regulatory requirements pursuant to Gramm-Leach Bliley for establishing a comprehensive Information Security and Risk Assessment Policy and Program

V. The Bank Secrecy Act

- a) A tool that the U.S. government uses against drug trafficking, money laundering, and other crimes. Establishes certain reporting and record-keeping requirements.
- b) Currency Transaction Reports
 - i) Currency transactions (deposit, withdrawal, exchanges transfers, etc) more than \$10,000
- c) Suspicious Activity Report
 - i) Any suspicious transaction relevant to a possible violation of law or regulation
 - ii) Transactions involving funds or aggregates of funds of at least \$5,000.00 which are derived from illegal activities
 - iii) Structuring (transactions designed to evade reporting requirements)
 - iv) Which have no business or apparent lawful purpose, or are not the sort of transactions that the particular customer would normally engage in, and for which there are no reasonable explanations after all available facts are considered.