



Anne E. Misback
Secretary, Board of Governors of the Federal Reserve System
20th St. and Constitution Ave NW
Washington DC, 20551

Re: Docket No. R-1564, Proposed Rule on Availability of Funds and Collection of Checks

Dear Ms. Misback:

Americans for Financial Reform (“AFR”) appreciates this opportunity to comment on the above-referenced proposed rule (“the Rule”) by the Federal Reserve Board (“the Board”) to adopt a presumption of alteration in disputes over whether a check has been altered or forged.¹ We support the proposed rule but urge the Board to clarify that the presumption be limited to disputes between banks and recommend the Board require banks to maintain original checks for a specified period of time.

Since the passage of The Check Clearing for the 21st Century Act (“Check 21”) which permits banks to substitute electronic images of checks for the original checks, electronic check processing has proliferated. As early as the third quarter of 2003, shortly after the passage of Check 21, over 60 million checks were truncated and processed electronically² By 2009, electronic image deposits accounted for over 96 percent of checks processed at Federal Reserve banks.³ Today, that number is even closer to 100 percent. This rapid shift from paper to electronic images is reflective of the general growing consumer preference for electronic payment methods.

Check 21 and the rise of electronic checks have benefited consumers and their banks in variety of ways, by reducing reliance on the check courier system and improving ease of payment and processing. However, they have also introduced new difficulties regarding check fraud. When paper checks are destroyed or otherwise truncated, they are replaced with lower-quality substitutes that cannot provide the full range of forensic information contained in the original. When handwriting, ink, fingerprints, etc. cannot be effectively examined, various aspects of check fraud become more difficult to prove. This is a problem when determining who should bear the loss when check fraud occurs. If finalized, the Rule would create a rebuttable presumption in disputed cases that a fraudulent check is altered rather than forged. This would

¹ Americans for Financial Reform is an unprecedented coalition of more than 200 national, state, and local groups who have come together to reform the financial industry. Our members include consumer, civil rights, investor, retiree, community, labor, faith-based, and business groups. A list of coalition members is available at <http://ourfinancialsecurity.org/about/our-coalition/>

² Lisa Wines, *Check Clearing for the 21st Century: Substitute Checks not Sufficient in Disputes Alleging Fraud*, 13 Syracuse Sci. & Tech. L. Rep. 95 (2006).

³ Paul Bauer, *The Check is Dead! Long Live the Check! A Check 21 Update* (Sept. 21, 2009), available at <https://www.clevelandfed.org/newsroom-and-events/publications/economic-commentary/economic-commentary-archives/2009-economic-commentaries/ec-20090609-the-check-is-dead-long-live-the-check-a-check-21-update.aspx>.

place the initial risk of loss on the depository bank. As previous commenters have noted, depository banks and their customers are usually the first to truncate and destroy paper checks. Depository banks are therefore in the best position to preserve original paper checks which can be used to overcome the proposed evidentiary presumption.

AFR urges the Board to ensure that the proposed presumption can only be applied in disputes between banks, not disputes between banks and their customers. Doing so would avoid shifting the risk of loss to the accountholder. Under UCC § 4-401, also known as the Properly Payable Rule, altered checks may still be paid according to their original terms. Consequently, unless this presumption of alteration is limited to disputes between banks, in some number of disputed cases, accountholders would be held at least partially liable for checks they did not write. Allowing the presumption to affect accountholder liability in this way is at odds with the UCC's established risk allocation framework which details the duties banks have to their customers. The Properly Payable Rule essentially makes banks strictly liable to their customers for any unauthorized transactions. Additionally, the UCC's presentment warranties seem designed to shift the risks of loss to banks and away from consumers in instances of fraud.⁴ Overall, the UCC framework appears to evince a strong policy in favor of minimizing accountholder loss. Neither this rule, nor any future rule the Board proposes should undermine that framework.

AFR also believes that the presumption of alteration should not apply if the bank asserting the presumption received and destroyed the original paper check. In such instances, the asserting bank – likely the drawee bank – is in the best position to preserve the original check and should properly bear the risk of loss associated with destroying it. To avoid this issue though, we recommend the Board require banks who receive original checks to preserve them for a set period of time so that they may be produced for inspection when disputes arise. The Bank Statement Rule found in UCC § 4-406 states that bank customers must be afforded up to 30 days to examine their bank statements for fraudulent transactions and notify the bank.⁵ It would be reasonable then for banks to be required to preserve paper checks for a period of up to 60 days. This would give consumers a chance to discover the fraud and allow banks to destroy checks after the window of time has closed for consumers to notify them.

Thank you for the opportunity to comment and your consideration on this matter.

Sincerely,
Americans for Financial Reform

⁴ UCC § 3-417; UCC § 4-208

⁵ UCC § 4-406(d)(2).