

A SODA SPECIAL REPORT 2005

"The Check 21 Act"

Check 21 is sweeping new federal law that takes away your ability to get back your original paper checks. Under this law, consumers will be more likely to bounce checks and may find themselves paying higher bank fees. The complicated new law gives you some rights, but those rights depend on a variety of factors, including how the merchant and the bank decide to process your check.

Tips from Consumers Union:

ASK FOR A RECREDIT IN WRITING: If something goes wrong with your checking account, make a written request that your bank "recredit" (return) the funds to your account. You have a right to recredit in some cases, and not in others. Because it is hard to tell when the right of recredit applies, you should ask, in writing, for a recredit whenever a check is paid twice, a check is paid for the wrong amount, or something else goes wrong with your checking account.

ASK FOR A SUBSTITUTE CHECK: You get a limited recredit right under Check 21, but the regulations restrict recredit to consumers who were provided with a substitute check. Always ask for a substitute check, which is a special kind of copy of your paper check. If you now get your original checks back, ask for an account that returns substitute checks every month. If your bank charges too much for an account that returns substitute checks every month, look for another bank.

EXPECT THE CHECKS YOU WRITE TO CLEAR FASTER: Don't write a check unless the funds are already in your account. The checks you write will clear faster, but banks aren't required to speed up the time when they make funds available from the checks that you deposit.

DON'T SIGN UP NOW FOR VOLUNTARY CHECK TRUNCATION: You have even fewer consumer rights under voluntary non-return of your checks than you'll have under Check 21. Decline invitations from your bank to convert to voluntary check truncation.

What are the main effects of "Check 21" on consumers?

- You won't be able to get your original paper checks back, because your bank will no longer have them.

- Checks you write will clear sooner, increasing the risk that a check will bounce if funds are not in the account when you write the check. Don't write a check unless the funds are already in the account to cover it.
- " You may not get access to the funds from checks you deposit any sooner, because the new law does not shorten check hold times. After 30 months, there must be a study on whether banks are making funds available to consumers earlier than the allowable hold periods.
- Banks will save money on processing checks, but banks are not required to share these savings with consumers.
- Different kinds of copies of a check will have different rights attached. Check 21 creates a new kind of paper copy of an electronic image of a check. This special kind of copy is called a "substitute check." Only a substitute check can be the legal equivalent of the original check, and only a substitute check triggers your right to recredit of disputed funds. A regular copy of a check does not carry these same protections. If you ask for a copy of a check, your bank may send you an ordinary copy instead of this special kind of copy which triggers legal rights and protections unless you ask for a substitute check.
- "A bank other than your bank will have your original check, and will decide whether to destroy it. Neither Check 21 nor other law requires a bank to keep your original check for any period of time. Before Check 21, your own bank decided how long to keep your original checks, if you didn't get them returned with your statement. Under Check 21, the bank of the person you wrote the check to may decide when to destroy your check.
- Consumers will get new rights for some electronically processed checks, but not for others. When a so-called "substitute check" is provided to a consumer, Check 21 gives the consumer a right to have funds of up to \$2,500 recredited to the consumer's account in 10 business days if the check is paid twice, paid for the wrong amount, or otherwise paid in error. The statute is ambiguous about whether this new right applies when a paper substitute check is used in the processing of the check but is not returned to the consumer.

The regulations restrict the right of recredit only to checks where the consumer was provided with a substitute check. If a check is processed electronically by all the banks it is routed through without the use of a substitute check and the consumer is not provided with a substitute check, then the check remains under state check law. In that case, the consumer does not receive a 10 day right of recredit even if the electronic image of the check is paid twice, paid for the wrong amount, or if both the electronic image and the paper check are paid.

- Consumers who want to maximize their consumer rights should ask for return of "substitute checks" with their checking account statements. Watch out for fees associated with a substitute check-returning account. Look for another bank if your bank charges a high fee to get copies of all your checks as substitute checks.

- Only the special "substitute check" can be legally equivalent to the original check to prove payment. The copies that a bank sends to consumers under a so-called "voluntary truncation" agreement, where the consumer agrees not to get the checks back, do not prove that a payment has been made, and do not trigger your Check 21 recredit right.

When do these changes go into effect?

Check 21 becomes effective October 28, 2004.

Can my bank continue to send me my original checks with my monthly statement?

No. Check 21 will make it impossible for consumers to get their original checks returned with a monthly statement, because Check 21 forces banks which now require the original check for processing to accept a special type of paper copy of an electronic image of the original check. This is called a "substitute check." Banks can give this special paper copy of the image of the check to consumers instead of the original paper check.

Under Check 21, the original check may stop at any bank in the collection chain. A bank can replace an original check with an electronic message containing the pertinent information if that bank and the next bank in the chain have an agreement to send and accept electronic presentment of checks.

Check 21 permits any bank to send a "substitute check" - a paper copy made from the original check or from an electronic image of the original check - to another bank even if that other bank only processes paper checks. Since the original check will no longer be returned to the consumer's bank, it will be impossible for the consumer to get his or her bank to simply return all original checks every month. The consumer's bank will no longer have all of those checks. Consumers who get their checks back now will experience a loss of convenience.

Will the substitute check be a full size check?

Not necessarily. The substitute check may be of any size, so long as it meets industry standards for a substitute check.

Is a substitute check as useful as an original check?

No. Certain substitute checks will be legally equivalent to an original check for all purposes under state and federal law. However, the substitute check will not be as useful as the original check for proving forgery or alteration, because it can't be used to determine pen pressure, and it is less useful for handwriting analysis.

Will all electronic images of checks be legally equivalent to an original check?

No. A consumer whose account agreement does not require the return of substitute checks may receive copies of electronic images, but those copies will not be legally equivalent to the original check. Check 21 does not require banks to offer an account that gives consumers substitute checks with their bank statements. In those states where banks are required by law to give consumers an option to receive their original checks back, banks will be able to send back substitute checks instead.

Does Check 21 require that the copies of checks banks send to consumers must meet any standards for size or readability if the copy is not a substitute check?

No. Existing state law requires that banks maintain a legible copy of checks for seven years, but not that the copies returned to consumers with statements be legible.

Does Check 21 require the bank to get and return an original check if the consumer requests that check?

No. Check 21 doesn't require banks to return even a single original paper check on request. However, if there is a dispute about whether the check was properly paid which requires the original check to resolve, then the bank may have to locate the original check if it does not want to resolve the dispute in the consumer's favor. If the consumer needs the original check for any reason other than a dispute with the bank, Check 21 creates no right to get that original check.

What will happen to the original checks under Check 21?

Check 21 does not impose any minimum time period on banks to keep original checks. Under state law, Uniform Commercial Code Article 4, original checks can be destroyed at any time, as long as the bank has the capacity to provide a legible copy of the check for seven years. UCC section 4-406(b).

Will a bank be able to use information from the electronic images of checks to invade the privacy of a consumer or a business?

Yes. Check 21 places no limits on a bank's use of information contained in its customers' check images. A bank might build a database using check images to determine which of its consumers shop at certain kinds of retailers, or what kinds of suppliers a business customer uses.

Who gets a choice under Check 21?

Check 21 offers maximum choice to banks, but not to consumers. Banks may continue to choose to process paper substitute checks rather than electronic images. A bank that wants to process paper can insist that from the prior bank in the collection chain send it a paper "substitute check," but not the original check, for processing. Consumers may no longer choose to get back their original checks.

Are there any benefits to consumers?

Yes, but consumers won't receive these benefits for all electronically processed checks. Check 21 gives a 10 business day right of recredit of disputed funds, up to the first \$2,500 of a check amount, but only if a special paper copy of the electronic image of the check (a substitute check) was provided to the consumer. However, a consumer who has received an ordinary copy of a check, not the special copy called a substitute check, does not have the right to recredit under Check 21 as it has been interpreted by the Federal Reserve Board's regulations. To trigger the right of recredit, a consumer will have to ask for and receive a substitute check.

What are the warranty and indemnity rights?

Check 21 is confusing. It gives you the remedy of a prompt right to recredit, but only if you were provided with a substitute check. Check 21 also gives you some rights if a substitute check was used but not provided to you, but you can't insist on a recredit within 10 business days to enforce those rights. Check 21 creates two warranties by the bank that creates the substitute check and by all later banks that transfer either the substitute check or a paper or electronic representation of it. The first warranty is a warranty (promise) that the substitute check is legally equivalent to the original check. The second warranty is that the check won't be presented for payment if it has already been paid (no double payment). There is also a limited indemnity when the consumer suffers a loss because a substitute check was used. The details of, and restrictions on, these rights are described in material posted by the National Consumer Law Center in the article, "***Banks Will No Longer Return Original Cancelled Checks***," posted at: <http://www.consumerlaw.org/initiatives/check21.shtml>.

Why do consumers need the right of recredit?

Consumers can be harmed in several ways by the processing of an electronic image rather than the original check. First, both the paper check and the electronic image might be paid (double payment). Second, transferring the check back and forth between paper and electronic formats creates a risk that the amount on the paper check might be changed when it is turned into an electronic image for processing. Third, it may be impossible to prove that a check has been forged or altered without the original check. The switch to electronic imaging of checks means that the original check would not be held by the consumer or the consumer's bank. Instead, one of the other banks in the collection chain would have the original check. It is likely to take longer to find the check, and to get it back if it has not been destroyed, than if the consumer or the consumer's bank were holding it. A recredit right means that the consumer, not the bank, has the use of the funds while waiting to resolve the dispute.

When do consumers get a recredit right under Check 21?

Check 21 gives a recredit right only when a substitute check is used. The regulations take an even narrower view of this right, restricting it to only where a substitute check was provided to the consumer. Federal law on other types of electronic payments, such as debit card payments, gives consumers a more complete right of recredit.

How long will it take to get the disputed funds recredited?

The recredit must occur within 10 business days after the banking day on which it is requested, plus the bank gets one extra business day to make the funds available. If the amount in dispute is more than \$2,500, only the first \$2,500 must be recredited in this time period.

Why didn't consumer groups support Check 21?

Consumers Union and other consumer groups believe that consumers should have a right to recredit for every check that is processed wholly or partly electronically. Check 21 does not accomplish this, and it leaves open opportunities for new bank fees and new types of invasions of consumer financial privacy. The Federal Reserve Board's regulations interpret the provisions of Check 21 very narrowly. Click here to read the comments filed by Consumers Union and other national consumer organizations about the problems with the proposed regulations on Check 21.

What can be done about this confusing situation?

Congress should amend the federal Electronic Fund Transfer Act to apply its consumer protections to every check that is processed wholly or partly by electronic means.

Where can I get more information?

For information from Consumer Reports about Check 21 and other payment methods, click [here](#).

For more information about Check 21, see "Banks Will No Longer Return Original Cancelled Checks," posted by the National Consumer Law Center, at: <http://www.consumerlaw.org/initiatives/check21.shtml>.

For the final federal regulations on Check 21, issued July 26, 2004.



**A Member
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Consumers Union and the Consumer Federation of America recommend seven policies banks and other financial institutions could adopt to improve Check 21 for consumers. Click [here](#) to read about these policies.

* **This has a dramatic effect on the way we do business.**

* **What Do You Need To Do ? Contact:**

<http://www.consumerlaw.org/initiatives/check21.shtml>.

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