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*Expedited Funds Availability/Check-Holds*

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**Abstract.** The 2003 enactment of P.L. 108-100 (the Check 21 Act) refocused attention on the check-hold policies of financial institutions. This act made it easier for financial institutions to convert paper checks into electronically generated images and was aimed at making the clearing process between institutions faster and more efficient. The law did not require institutions to generate or receive check images, but required them to accept substitute checks created from electronic images. Consumer advocates were concerned that the implementation of Check 21 would result in money clearing out of accounts faster without speeding up the availability of funds deposited into accounts. Check 21 required the Federal Reserve to study and evaluate the impact of the act on the clearing process. In April 2007, the Federal Reserve issued a report to Congress on the results of such a study. The Federal Reserve recommended making no changes to the prevailing funds availability policies. Consumer advocates continued to urge Congress to reduce check holds by amending the EFAA. On September 16, 2008, the House Financial Services Committee ordered to be reported the Expedited Funds Availability Dollar Limits Adjustment Act of 2008 (H.R. 6871). This bill would make adjustments to the check-hold provisions of the EFAA.

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## CRS Report for Congress

### Expedited Funds Availability/Check-Holds

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#### Summary

In 1987, Congress passed the Expedited Funds Availability Act (EFAA),<sup>1</sup> which addressed the check-hold policies of depository financial institutions for various types of transaction accounts. The act was meant to ensure timely access to deposited funds and requires institutions to disclose to customers their funds availability policies. Federal Reserve Regulation CC implements the funds availability provisions and includes a schedule with maximum time limits for withholding funds.

The 2003 enactment of P.L. 108-100 (the Check 21 Act)<sup>2</sup> refocused attention on the check-hold policies of financial institutions. This act made it easier for financial institutions to convert paper checks into electronically generated images and was aimed at making the clearing process between institutions faster and more efficient. The law did not require institutions to generate or receive check images, but required them to accept substitute checks created from electronic images. Consumer advocates were concerned that the implementation of Check 21 would result in money clearing out of accounts faster without speeding up the availability of funds deposited into accounts. Check 21 required the Federal Reserve to study and evaluate the impact of the act on the clearing process. In April 2007, the Federal Reserve issued a report to Congress on the results of such a study. The Federal Reserve recommended making no changes to the prevailing funds availability policies. Consumer advocates continued to urge Congress to reduce check holds by amending the EFAA. On September 16, 2008, the House Financial Services Committee ordered to be reported the Expedited Funds Availability Dollar Limits Adjustment Act of 2008 (H.R. 6871). This bill would make adjustments to the check-hold provisions of the EFAA.

This report will be updated as events and legislation warrant.

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<sup>1</sup> P.L. 100-86; 101 Stat.563.

<sup>2</sup> 117 Stat.1177.

## Background

The intent of the Expedited Funds Availability Act (EFAA) of 1987 was twofold: first, to ensure that account holders have timely access to deposited funds; and second, that depository financial institutions provide to their customers clear disclosure about check hold policies. The practice of placing holds on accounts was developed to protect an institution in the event a deposited check was returned unpaid. Provisions of the 1987 act addressed the need for improvements in the check collection and return system to counter the effect of reduced hold periods.

The potential costs to account holders from lengthy hold periods and insufficient disclosure of hold policies provided the impetus for this legislation. During a hold period, customers are unable to make withdrawals by check or other means against those deposited funds on which the hold was placed. If a financial institution receives a check written against an account before the hold is lifted and the account has insufficient funds because of the hold, it can choose to cover the check and charge the customer an “overdraft” fee. Alternatively, the institution can return the check without paying it and charge the account holder a “bounced check” or “nonsufficient funds” fee. The third party check recipient may charge the account holder an additional “returned check” fee. As it is possible for more than one check to be presented during the hold period, the fees can accumulate quickly.

The Federal Reserve’s Regulation CC implements the EFAA.<sup>3</sup> Regulation CC applies to all transaction accounts (as defined by Federal Reserve Regulation D) and it extends to both consumer- and business-held deposit accounts. The regulation does not require check holds. The check hold policies of depository financial institutions can vary within the restraints of maximum time frames that are outlined in a schedule. The regulation also provides for longer hold periods under “exception” situations. Regulation CC contains rules for disclosure of funds availability policies and to expedite the return of unpaid checks by institutions.

The schedule is measured in business days following the banking day of deposit, and all references are to the maximum number of days that a financial institution can hold a check deposit. The first \$100 of any check deposit must be made available the first business day following the day of deposit. Several types of check deposits are subject to “next-day availability,” which means that funds must be available the first business day following the banking day of deposit. In this category are U.S. Treasury checks and the following checks when deposited in person: cashier’s, certified, or teller’s checks, U.S. Postal Service money orders, Federal Reserve Bank or Federal Home Loan Bank checks, state or local government checks, and checks drawn on another account held by that institution (“on-us checks”). The time period is extended when deposits are made at an ATM (automated teller machine). If the ATM is owned by the account holder’s financial institution, the funds must be available by the second business day. Deposits made at ATMs owned by other institutions must be available by the fifth business day.

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<sup>3</sup> 12 CFR 229. The full text is available at [[http://ecfr.gpoaccess.gov/cgi/t/text/text/-idx?c=ecfr&sid=635f26c4af3e2fe4327fd25ef4cb5638&tpl=/ecfrbrowse/Title12/12cfr229\\_main\\_02.tpl](http://ecfr.gpoaccess.gov/cgi/t/text/text/-idx?c=ecfr&sid=635f26c4af3e2fe4327fd25ef4cb5638&tpl=/ecfrbrowse/Title12/12cfr229_main_02.tpl)] and by way of [<http://www.federalreserve.gov/bankinforeg/relisting.htm#CC>].

In general, if a check is not subject to “next day availability” the clearing schedule (except for the first \$100) depends on whether the check is local or nonlocal. If the account holder’s institution is in the same check processing region as the paying institution,<sup>4</sup> the check is local. Funds deposited by local checks must be made available for withdrawal by the second business day and alternatively, funds from nonlocal checks must be made available by the fifth business day.

Regulation CC also permits financial institutions to impose “exception” holds for certain types of deposits or accounts. Included in the exception category are large deposits (greater than \$5,000), redeposited checks, deposits to accounts repeatedly overdrawn, when the institution has a reasonable cause to doubt the collectibility of the check, emergency conditions, and new accounts (open less than 30 days). In general, the extended period of time for on-us checks is one additional business day (for a total of two days), for local checks five additional business days (for a total of seven days), and for nonlocal checks six additional business days (for a total of eleven days). However, the financial institution shall make \$400 of the deposited funds available by 5:00 pm on the business day on which the funds would have cleared if the exception had not been imposed. The \$400 is in addition to the first \$100.

Regulation CC requires financial institutions to provide customers with a written disclosure of their funds availability policies prior to opening a transaction account. If the availability terms on an existing account are changed, the account holder must be provided with a new disclosure 30 days in advance unless the change expedites the availability of funds, in which case, notice may be given no later than 30 days after implementation. In addition, notices must be posted in each location where employees accept deposits and at all ATMs. The customer must be notified when an exception hold is placed on a deposit. Model disclosure statements are provided.

The regulation contains provisions to speed up the check-return process in an effort to ensure that institutions are advised when a check is being returned before the deposited funds are made available. Options and methods are addressed in Subpart C of Regulation CC. In general, institutions are encouraged to use the most efficient path to route the return and to provide for the automated processing of returned checks. Finally, the Board of Governors of the Federal Reserve is directed by Section 603 (d) (1) of the EFAA to make reductions in the hold time periods established in Regulation CC as warranted by improvements in the check clearing system.

## Issues Raised By Check 21

The Check Clearing for the 21<sup>st</sup> Century Act (P.L. 108-100), commonly referred to as Check 21, was enacted on October 28, 2003, to foster innovation in the payments system and enhance its efficiency by facilitating the use of electronic check processing.<sup>5</sup>

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<sup>4</sup> Party responsible for making the payment of the amount written on a check.

<sup>5</sup> For more information, see CRS Report RL32668, *Electronic Banking: The Implementation of the Check 21 Act*, by Walter W. Eubanks and CRS Report RS22525, *Electronic Banking: The Post-Check 21 Payments System*, by Walter W. Eubanks.

The implementation of the act has raised concerns with the current check-hold time periods permitted by Regulation CC and whether they should be adjusted.

## Overview of Check 21 Act

Check 21 deals with the check collection process, and its purpose is to enable financial institutions to handle more checks electronically. The law does not require institutions to adapt new collection procedures or generate digital check images, but it does require institutions to accept a new negotiable instrument, a paper “substitute check,” created from the electronic information captured from the original paper check. It was anticipated that the Check 21 Act would not result in an immediate transformation, but in a gradual evolution away from a paper-based payments system. Therefore, the benefits from electronic check processing might not be immediately realized.

P.L. 108-100, the Check 21 Act, required the Federal Reserve to conduct a study of

- the percentage of total checks cleared in which the paper check is not returned to the paying bank;
- the extent to which banks make funds available to consumers for local and nonlocal checks prior to the expiration of maximum hold periods;
- the length of time within which depository banks learn of the nonpayment of local and nonlocal checks;
- the increase or decrease in check-related losses over the study period; and
- the appropriateness of the time periods and amount limits applicable under sections 603 and 604 of the Expedited Funds Availability Act, as in effect on the date of enactment of [the] Act.<sup>6</sup>

The act also required the Board to report the results of the study, together with recommendations for legislative action. The Board submitted the required report to Congress in April 2007. (See discussion below.)

## Check Processing Issues

Consumer advocates have raised several issues with Check 21. A major concern has been that although the electronic check processing facilitated by this act would greatly reduce the time it takes to deduct money from a customer’s account, the act would not improve the account holder’s access to the deposited funds. Therefore, they have argued, the benefits from the increased use of electronic processing would accrue mainly to banks. Legislation (H.R. 799) to address this potential imbalance was introduced in the 109<sup>th</sup> Congress on February 15, 2005. H.R. 799 would have amended the Expedited Funds Availability Act to reduce the maximum time frames for hold policies. Other adjustments addressed in the legislation included raising the threshold for large check exceptions from \$5,000 to \$7,500, treating Saturday as a business day if accounts are debited on Saturdays, and requiring institutions to process credits before debits. The bill was referred to the House Committee on Financial Services, but no further action was taken.

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<sup>6</sup> P.L. 108-100, 16.

In April 20, 2005, the House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit of held an oversight hearing on the implementation of the Check 21 Act.<sup>7</sup> Among the issues addressed was whether to revise funds availability schedules. The Federal Reserve testified that material improvements from Check 21 had not yet been realized. The banking industry representatives testified that the transition to electronic check processing would be gradual, and that the provisions of Check 21 facilitate a gradual and orderly change. In addition, check hold policies continued to provide protections against check fraud.

The consumer advocate testified that the Check 21 Act and advances in technology have facilitated more efficient check processing. According to this testimony, changes to the funds availability schedules should not have to wait until the vast majority of checks are processed electronically. Congress was urged to reduce check holds by amending the EFAA if the Federal Reserve's 2007 report did not recommend changes in hold times.

## April 2007 Federal Reserve Report

In April 2007, and pursuant to P.L. 108-100, the Federal Reserve submitted a report to Congress on the effects of the Check 21 Act on the nation's check collection system.<sup>8</sup> In March 2006, the Board of Governors of the Federal Reserve System conducted a survey of the banking system to assess whether there had been sufficient improvement in the check collection and return system to support changes to the funds availability schedules. Based on the survey findings and other research gathered by the Board, the Board recommended making no changes to the current funds availability policies.

At the time of the survey Check 21 had been in effect for 17 months. The March 2006 survey identified a slow-paced adoption of Check 21 by financial institutions. The survey results indicated that approximately 93% of all checks paid involved a paper check.<sup>9</sup> The Federal Reserve's report did state that by January 2007 the nation's banking industry had experienced a significant increase in the use of electronics to collect and present checks for payment. The report also concluded that Check 21 was an important catalyst for potential change but much broader adoption of new technologies and processes must occur before check return times can decline appreciably.

The report also addressed the effect on check holds of the consolidation of the Federal Reserve's check-processing sites. The Federal Reserve had begun a program of reducing the check-processing infrastructure in response to declining check volumes.

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<sup>7</sup> U.S. Congress, House Committee on Financial services, Subcommittee on Financial Institutions and Consumer Credit, Implementaion of the Check Clearing for the 21<sup>st</sup> Century, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., April 20, 2005, serial no. 109-20 (Washington, DC: GPO,2005). Available at [<http://financialservices.house.gov/archive/hearings.asp@formmode=detail&hearing=374.html>].

<sup>8</sup> Board of Governors of the Federal Reserve System, "Report to the Congress on the Check Clearing for the 21<sup>st</sup> Century Act of 2003," April 2007 (Washington, DC:2007). This report can be viewed at [<http://www.federalreserve.gov/boarddocs/RptCongress/check21/check21.pdf>].

<sup>9</sup> Ibid. p. 10.

When check-processing regions are combined into one larger region, the result is a change in the classification of a number of deposited checks from nonlocal to local. This reclassification reduces the maximum permissible hold periods for that volume of checks now deemed local. The report stated that additional consolidations were expected.

Finally, the Board would continue to monitor the check collection and return system and would use its existing authority, consistent with EFAA, to accelerate funds availability schedules when the evidence warranted. As mentioned above, the Board of Governors of the Federal Reserve is directed by Section 603 (d) (1) of the EFAA to make reductions in the hold time periods established in Regulation CC as warranted by improvements in the check clearing system.

## H.R. 6871

The Expedited Funds Availability Dollar Limits Adjustment Act of 2008 (H.R. 6871) was introduced on September 11, 2008, by Representative Carolyn Maloney, co-sponsored by Chairman Barney Frank, and referred to the House Committee on Financial Services. H.R. 6871 would amend the EFAA with the intent to improve the account holder's access to their deposited funds. Representative Maloney stated that the Federal Reserve Board was supportive of the dollar adjustments contained in the bill.<sup>10</sup>

The bill would make a one time adjustment to two withdrawal dollar amounts addressed by Section 603 of the EFAA; it would

- make an adjustment to the current requirement that the first \$100 of any check deposit be made available the first business day following the day of deposit by increasing the amount from \$100 to \$175; and
- change the amount of funds financial institutions must make available when imposing an "exception" hold on deposits from \$400 to \$700.

In addition, H.R. 6871 would require the Federal Reserve Board to make regular future adjustments based on inflation.

On September 16, 2008, the committee ordered the bill to be reported. No further action has been taken.

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<sup>10</sup> See September 16, 2008, Rep. Maloney press release available at [[http://maloney.house.gov/index.php?option=com\\_content&task=view&id=1715&Itemid=61](http://maloney.house.gov/index.php?option=com_content&task=view&id=1715&Itemid=61)].