

**SCHWARTZ & BALLEN LLP**  
1990 M STREET, N.W. • SUITE 500  
WASHINGTON, DC 20036-3465  
(202) 776-0700

FACSIMILE  
(202) 776-0720

www.schwartzandballen.com

**MEMORANDUM**

July 27, 2004

To Our Clients and Friends

Re: Final Rule Implementing the Check 21 Act

On July 26, 2004, the Board of Governors of the Federal Reserve System (the “Board”) released its amendments (the “Final Rule”) to Regulation CC to implement the Check Clearing for the 21st Century Act (“Check 21 Act”). The Final Rule includes both the implementing regulation and related commentary, as well as a model consumer awareness disclosure and other model notices.

The Final Rule is effective on October 28, 2004. The model consumer awareness notice is effective immediately, and provisions relating to the use of black ink on indorsements are effective on January 1, 2006.

**FINAL RULE**

The Final Rule sets forth a number of clarifying changes in response to comments received, but is substantially similar to the proposed rule that the Board issued for comment in December of 2003.

The Check 21 Act, as implemented by the Final Rule, authorizes a new negotiable instrument called a “substitute check.” A substitute check is a paper reproduction of an original check that contains an image of the front and back of the original check and can be processed like the original check. By authorizing the use of a substitute check, the Check 21 Act allows for a broader use of electronic check processing without making it mandatory that banks change their current check collection practices.

Provisions of the Final Rule include:

- Legal equivalency of a substitute check. A substitute check is the legal equivalent of an original check if it accurately represents all of the information on the front and back of the original check and if it bears the legend stating: “This is a legal copy of your check. You can use it the same way you would use the original check.”
- Warranties. A bank that transfers, presents or returns a substitute check warrants to parties that the substitute check is a legal equivalent of the original, and that no depository bank, drawee, drawer or indorser will be asked to make a payment based on a check that it has already paid.
- Indemnities. A bank that transfers, presents or returns a substitute check for which it receives consideration indemnifies the recipient for any loss incurred by any recipient of a substitute check, if the loss occurred due to the receipt of a substitute check and not the original check.
- Expedited recredit process for consumers. A consumer may make an expedited recredit claim with respect to a substitute check if the substitute check was not properly charged to the consumer’s account. The Check 21 Act and the Final Rule establish time frames and prerequisites for the filing of an expedited recredit claim by a consumer and the resolution of the claim by the bank.
- Consumer awareness notice. A bank must provide a consumer awareness disclosure to each of its consumer customers that describes that a substitute check is the legal equivalent of an original check and that the consumer recredit rights apply when a consumer believes that a substitute check was not properly applied to the account. A bank shall provide the disclosure to each consumer who receives paid checks in periodic account statements. If a consumer requests a paid check and receives a substitute check, banks also shall provide the consumer with a disclosure.

The Final Rule also provides guidance on a number of issues that were raised during the consideration of the proposed rule, including:

- expressly recognizing the American National Standard Specifications for an Image Replacement Document – IRD, X9.100-140 as the applicable industry standard for substitute checks;
- permitting the MICR line on a substitute check to vary from the MICR line on an original check in accordance with industry standards; and

- clarifying that brokerage accounts and credit card accounts are not consumer accounts under the Act or Final Rule.

The final rule can be found at [http://www.schwartzandballen.com/whats\\_new.html](http://www.schwartzandballen.com/whats_new.html).

If you have any questions, please call Gilbert Schwartz, Robert Ballen or Tom Fox at (202) 776-0700.