

# Regulations for All Payment Systems

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# What are we Talking about Today...

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The major payment systems

Regulations – Regulations – Regulations

Laws – Laws – Laws

Rules – Rules - Rules

Private sector agreements and how/when they apply

# The Legal Structures of Payments in the U.S.

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## Wire Transfer Systems—

- UCC Article 4A
- Federal Reserve Reg J and OC6
- Private sector agreements and rule sets
  - CHIPS and SWIFT

## Checks—paper and electronic

- UCC Article 3 & 4
- Federal Reserve Reg CC, Reg J, and OC3
- Private sector “rules”--ECCHO

# Payment Systems Legal Structure

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## Automated Clearing House

- Private sector rules--Nacha
- Formats developed and owned jointly
- All operations and services by FedACH and EPN
- Federal Reserve Bank OC 4
- Public laws that apply: EFTA/Reg E, UCC 4A

## Cards—debit & credit

- Primarily structured by “agreement” — overlay of consumer protection regs (TILA; EFTA; Durbin)

# Payment Systems Legal Structure

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## Faster/Instant Payments

- Private sector rules-RTP
- Federal Reserve Bank OC 8
- Public laws the apply: EFTA/Reg E, UCC 4A

# Public law v. Private Sector Agreements

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## What's covered by public law

- Consumer protection
- Wire & Checks
- Dealing with public institutions—e.g. FRBs
- Crimes—fraud, BSA/AML, etc.

## What's left to private sector agreements

- ACH
- Check images
- Standards & nuts & bolts of operations



# Quick Reference Guide

<b><u>ACH</u></b>	<b><u>Check</u></b>	<b><u>Cards</u></b>	<b><u>Wire</u></b>	<b><u>Other</u></b>
ACH Rules	UCC Article 3	Regulation E	UCC Article 4A	BSA
31 CFR 210	UCC Article 4	Regulation Z	Regulation J	OFAC
Regulation E	Regulation CC	Card Network Rules	Operating Circular 6	E-Sign
UCC Article 4A	Operating Circular 3	PCI	CHIPS	Regulator Guidance
Operating Circular 4	Regulation J	Card Act of 2009	Contract Law	Contract Law
Regulation CC	Clearing House Rules - ECCHO	Durbin – Regulation II	Compensation	Much More
Regulation D	Contract Law (Image)	Contract Law	Regulation E for Consumer International	
Contract Law		EMV		

# The Rule Makers

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Laws – Federal & State

Federal Reserve Banks

Federal Reserve Board of  
Governors

CFPB

Other  
Regulators

Private Sector Networks

- Nacha
- ECCHO
- Cards/ATM
- TCH

# Which One Wins?

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When it **Appears** there is a conflict between Rules/Laws & Regulations the Alphabet Wins!

Unless it works to the accountholders favor

2 scenarios:

- Regulation CC funds availability on ACH Credits is next Day
- Nacha Operating Rules – funds availability is Settlement Date
- Regulation E – credit/provisional credit for “unauthorized entry” = 10 days
- Visa – requires Visa issuers to credit within = 5 days





# Check History

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Essence of check: Paper payment order



Electronic processing—  
1960-1990

MICR—paper check as “IBM card”  
Electronic presentment under 4-110



Escapes from paper—post  
1990:

Check to ACH—NACHA Rules & Reg E  
•CheckACH Coalition; DCT Pilot  
Image exchange—ECCHO Rules  
C21 Act facilitates image exchange  
•Hugely successful—but not all consequences were  
foreseen

# Checks – State Contract Law

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## UNIFORM COMMERCIAL CODE ARTICLE 3

### Negotiable Instruments

- Definitions
- Negotiation
- Liability
- Presentment Warranties

### UCC 3 –

- Assigns Depository Bank liability
- Altered/Improper Payee

## UNIFORM COMMERCIAL CODE ARTICLE 4

### Deposits & Collections

- Processing, presentment
- Right to Stop Payment
- May pay Stale Dated items
- Liability

### UCC 4 –

- Assigns Paying Bank liability
- Counterfeit/Forged Maker signature

# Checks-Regulation CC

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Expedited Funds Availability Act & Check Clearing for the 21st Century

1998/2004/2006/2018

Consumer & Corporate

Checks, Substitute Checks, Images

Funds Availability

Collection of Checks

Implemented by Regulation CC

Funds Availability

- Checks, Wires, ACH
- Does not apply to Remote Deposit Checks

Collection of Checks

- Return Timeframes
- What's timely

Substitute Checks

Remotely Created Checks

- Assignment of liability to Bank of First Deposit

Exchange of Images

- Still considered by "agreement"
- Referred to as "electronic check"

Regulation CC jointly issued by Federal Reserve Board of Governors & Consumer Financial Protection Bureau

# Checks – Regulation CC

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Timely return – Received by Depository Bank by **2:00 pm** second business day following presentment



Increases to Funds Availability



Large Dollar Notification increased to **\$5,000**

Return of the Check can be notification



Protection for Duplicate Presentments + party holding the **Paper**

Restrictive Endorsement – over to the financial institution  
“Protection” for financial institutions accepting checks  
Not Required



# The Check 21 Act

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Check Clearing for the 21st Century Act, or “Check 21”



Effective on October 28, 2004



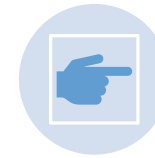
Implementing Regulations:  
New Subpart D to Regulation CC



Check 21 facilitates truncation and image exchange but does not govern it



Check 21 only creates and governs the use of a new negotiable instrument called a “substitute check” that can be used in place of the original without the agreement of the recipient



Check 21 provides new warranties and indemnities that flow with a substitute check and a copy or electronic representation of a substitute check



Subpart D to Reg CC covers electronic checks, substitute checks & derivatives

# What Doesn't Check 21 Do?

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Does not mandate that banks receive check images



Does not mandate that banks send check images



Does not mandate that banks that give customers check images provide “substitute checks” upon customers’ request, however, bank can still provide image copies of checks

# Checks-Regulation J

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Provides legal framework for DFIs to collect checks and other items and to settle balances through the Fed

- References Reg CC: Definitions of electronic check and electronic returned check and other terms
- References Uniform Commercial Code (UCC): For terms not defined in regulation

Specifies terms and conditions under which FRBs will receive items for collection from, and present items to, depository institutions

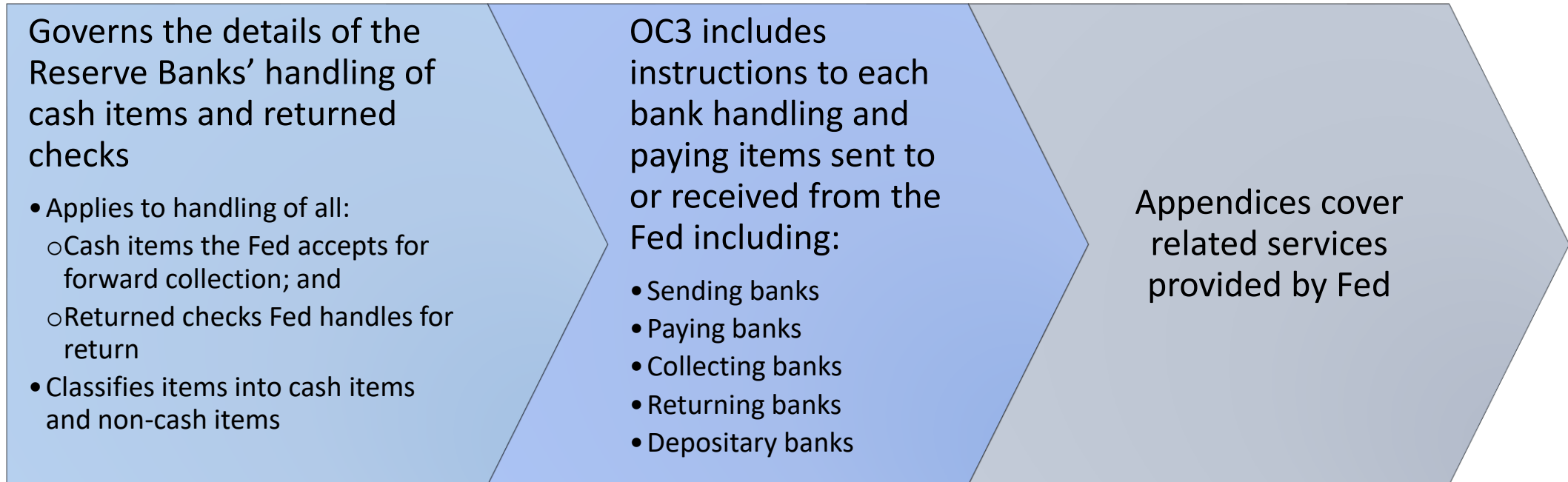
- Supplemented by operating circulars issued by the Reserve Banks

Used in conjunction with Reg CC to establish rules under which DFIs may return unpaid checks through the Fed

- Provides rules for collecting and returning items and for settling balances via accounts on the books of a Reserve Bank

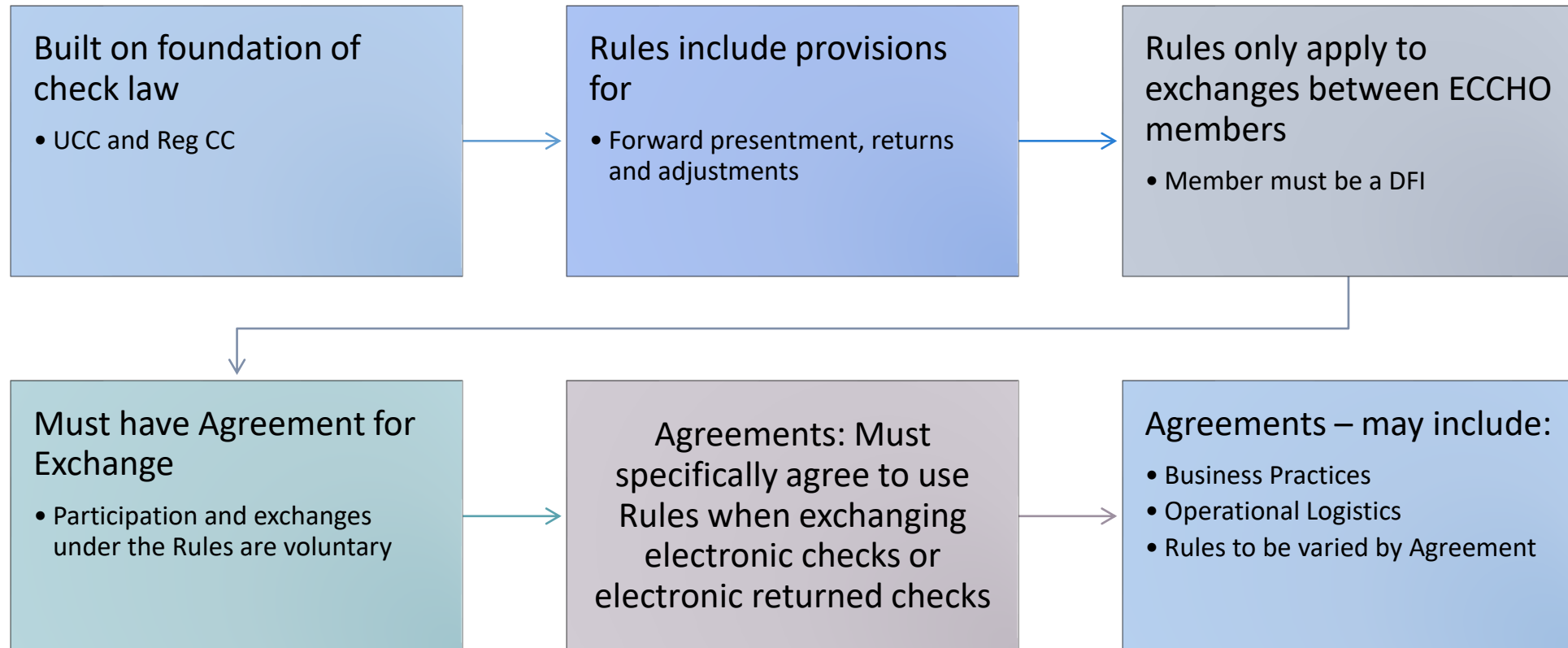
# Checks-Operating Circular 3

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# Private Sector Rules-ECCHO

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# Checks – When Things Go Wrong

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## ADJUSTMENTS

Correction of Errors

FRB & ECCHO

Timing & Entry requirements

Example

- Duplicate Presentments
- Amount Errors
- Non-cash items presented

## DISPUTES & WARRANTY BREACHES

Who is on the hook

Process to resolve

Typically, directly between the parties

No defined timeframe for resolution

Who is on the hook for the issue

**WHEN THE DIRECT DEPOSIT**



**HIT YOUR BANK  
ACCOUNT**

mematic.net

**I WAS TOLD**



**THERE WOULD BE DIRECT  
DEPOSIT**

mematic.net

# ACH History

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## Early 1970's

- SCOPE and the first ACH association
- Regional associations & Reserve Banks
- Government Direct Deposit – 1975 Green Book

Regional to national: NACHA & FedACH

1980's—recurring payments, limited actors

Late 90's--“New” ACH: one time payments; check to ACH conversions; more actors

2000's—same day ACH

Looking forward...faster payments? Dollars/data value proposition? Direct exchanges versus comprehensive network?



# ACH – Governing Rules

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Nacha Operating Rules

Governs ACH entries transmitted thru an ACH Operator

Contract Law

Warranty Based

New “color” every year

You Agree, you Follow, you get to Play

Nacha serves as the “Rule-making” entity

Rules voted on by the Direct Financial Institution members and Payment Associations (Macha)

# ACH – Governing Law – Federal Payments

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Single Largest User of the ACH

The Law – 31 CFR Part 210

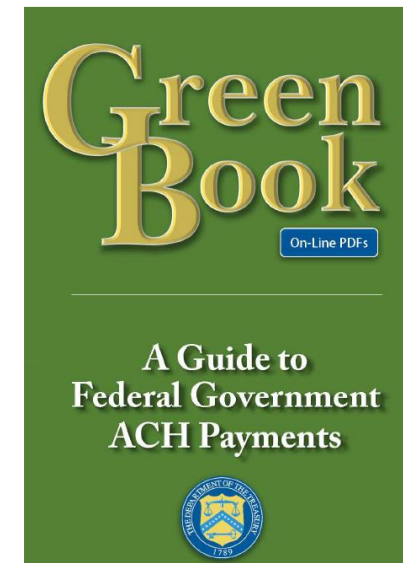
1999 – Officially adopted the Nacha Operating Rules

With certain exceptions:

- Liabilities & Warranties
- Federal Benefit Payment Reclamations
- Rules Enforcement (not subject to fines)

Green Book

- Serves as the “procedure manual” for financial institutions



<https://www.fiscal.treasury.gov/reference-guidance/green-book/>

# Federal Government ACH Payments

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Social Security Benefits (SSA and SSI)

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Veterans Benefits

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Railroad Retirement Benefits

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Civil Service Retirement/Federal Salary/Travel Reimbursements

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Disaster Assistance Payments

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Vendor Payments

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Tax Refunds

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Grant Payments

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Department of Defense (Non-Treasury Disbursed)

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# Moving the Money and the Message

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## Federal Reserve Bank – Operating Circular # 4

- Governs clearing & settlement of ACH thru FRB
- Defines:
  - Hours of ACH Operations
    - 3:00 am – 2:15 am
  - Settlement:
    - 8:30 am ET
    - 1:00 pm ET
    - 5:00 pm ET
    - 6:00 pm ET

# ACH – Regulations & Statutes

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## REGULATION E

### **Consumer** ACH Entries

- Terms & Conditions
- Reporting
- Error Resolution

*Of Note: There is no conflict between Regulation E's timeframe for reporting an error and the Nacha Operating Rules that allow an RDFI to automatically return an ACH entry.*

## UCC ARTICLE 4A

### **Corporate** ACH Credits

- CCD/CTX/IAT to Corporate Account
- Transactions flow thru ACH
- Provisional Credit Until Settlement
- Immediate Notice Not Provide
- If Settlement not received, Receiver refunds RDFI
- Choice of State Law



**GIVE ME THE  
CREDIT CARD**

**NO USE A  
DEBIT CARD**

# Cards- Plastic Everywhere

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## Payment System Rules

- ATM Networks
  - Star
  - Pulse
  - Shazam
  - etc.
- Card Brands
  - Visa
  - Mastercard
  - Discover
  - American Express

## Regulation II

- Durbin Amendment
- Caps on Debit Interchange
- Routing choice by Merchant

## PCI

- Payment Card Industry Data Security Standards
- Data protection of card information

# Cards – Consumer Protection

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## Regulation E

- Debit Cards
- Consumers
- Overdraft
- Terminals
- Consumer Liability

## Regulation Z

- Consumer
- Extension of Credit
- Disclosures
- Crediting of Payments
- Error Resolution

## Card Act 2009

- Transparent practices in extending credit
- Gift Cards
- Prepaid Cards

## CFPB

- Prepaid Card Regulations
- Updates to Regulation E & Z
- Compliance guide is **158** pages
- Significant requirements – disclosures, fees, errors



# Cards – Consumer Rights

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## Regulation E

- Does not provide protection for credit cards-Debit Card only
- Unauthorized
- Amount error
- Incorrect ATM Dispense
- A few other issues
- Consumer gives authority to another to use – lose their protections

# Network Rules-VISA and Mastercard

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## **Zero Liability – better than Regulation E**

- Unauthorized
- You must honor

## **Card Networks**

- Additional provisions for
- Goods not received
- Goods defective
- Refund not received
- What I call “Contract Disputes”
- These are not Regulation E issues

# Cards - EMV

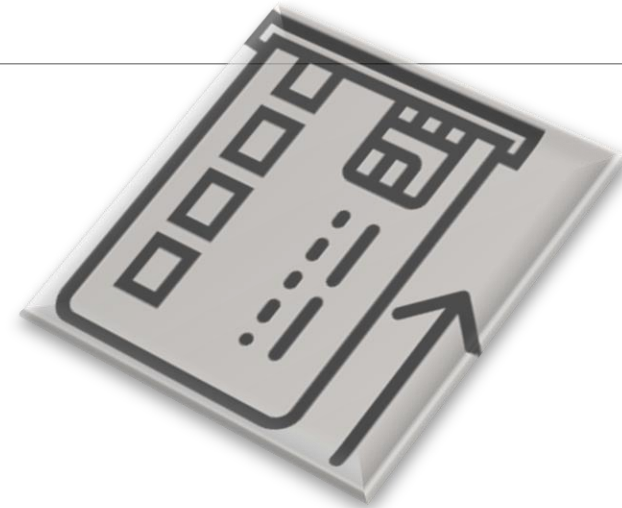
## EMV

**Dynamic transaction data creates unique transaction each time**

**Strong defense for Counterfeit – In-Person Fraud**

**In the US – Chip and Choice**

**Card Fraud is not going away – just shifting to Card Not Present**



<b>Whose Compliant</b>	<b>Merchant</b>	<b>Issuer</b>	<b>Liability</b>
EMV Ready	Yes	No	Issuer
EMV Ready	No	Yes	Merchant
EMV Ready	Yes	Yes	Issuer
EMV Ready	No	No	Issuer

**ME WAITING**



**FOR A WIRE TRANSFER**

[makeameme.org](https://www.makeameme.org)

# Wire Transfer - Systems

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## FedWire

- Federal Reserve Bank
- US Financial Institutions

## CHIPS

- The Clearing House
- Private = 50 Participants
- 1.5 Trillion per day

## SWIFT

- International Messaging
- Does not “actually” move money

Credit Only  
Transactions

Final when Sent!

<b>Uniform Commercial Code Article 4A</b>	<b>Regulation J Subpart B</b>	<b>FRB Operating Circular # 6</b>	<b>CFPB Regulation E Remittance Rules</b>
Consumer & Corporate Accounts	Between Financial Institutions & Federal Reserve Banks	FedWire Operations	<b>Consumer International Wires</b>
Assignment of Liability	Rights & Obligations of FRB	Security	More than 500 per year, FI must comply
Some Provisions can be varied by agreement	Sending & Receiving Institutions	Processing & Settlement	Disclosures, Fees, Error Resolution

# Wire Transfer – Laws, Rules, Regulations

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# Wire Transfers – Keeping it Legal & Safe

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# Wire Transfers - Errors

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## Interest Compensation

- Example FI receives a Wire – cannot post
- But the Wire is not “returned” for several days
- Sending FI might ask for “Interest” compensation

## Considerations

- UCC Article 4A - 207
  - Receiving FI can post based on Account Number Only
  - But, if Receiving FI “knows” there is a name mismatch
  - You might not be able to accept
- UCC Article 4A-209
  - Provision that cannot be varied by Agreement
  - Obligation to credit Beneficiary if Wire Transfer is “Accepted”



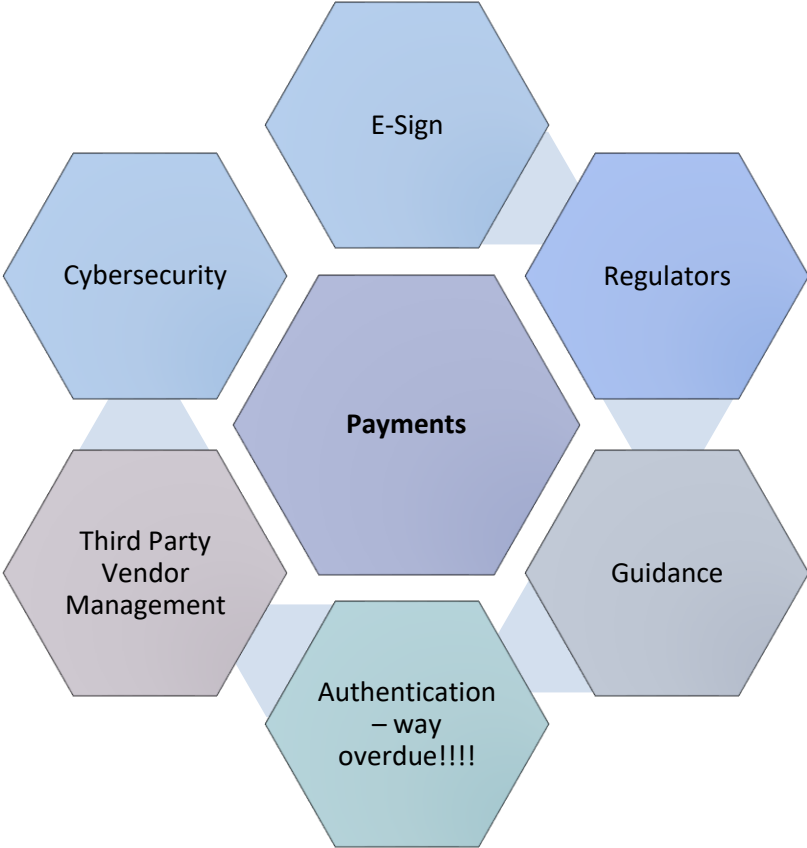
# All the Flavors of Faster Payments

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# More to Consider

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# Resources

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Nacha Operating Rules

Green Book - <https://www.fiscal.treasury.gov/reference-guidance/green-book/>

UCC Articles

- [www.law.cornell.edu/ucc](http://www.law.cornell.edu/ucc)

Regulations / Operating Circulars

- [www.federalreserve.gov](http://www.federalreserve.gov)
- [www.frbservices.org](http://www.frbservices.org)
- [www.ecfr.gov](http://www.ecfr.gov)
- [www.consumerfinance.gov](http://www.consumerfinance.gov)

Regulatory Agencies - Guidance

- FTC, OCC, FDIC, FRB, NCUA, CFPB
- [www.ffiec.gov](http://www.ffiec.gov)

# For Your Records

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Regulations for All Payment Systems

June 27, 2024

This session is worth 1.8 credits



# Payments – It's What We Do!

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Macha – Everything Payments - Everywhere

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