

Check 21 Promises Greater Choices, Efficiency, Innovation

Although volume is declining, checks remain the most popular form of non-cash U.S. retail payments, and it's no secret that the current check collection and return process is both costly and labor-intensive. Good news – help is on its way.

Legislation known as the Check Clearing for the 21st Century Act, or Check 21, will assist financial institutions in taking greater advantage of electronic check clearing and return capabilities. In December 2001, the Federal Reserve proposed legislation to Congress that would remove some legal impediments to check truncation with the goal of fostering innovation and efficiency in the payments system. The President signed Check 21 into law on October 28, 2003. The provisions of Check 21 will take effect 12 months after passage on October 28, 2004.

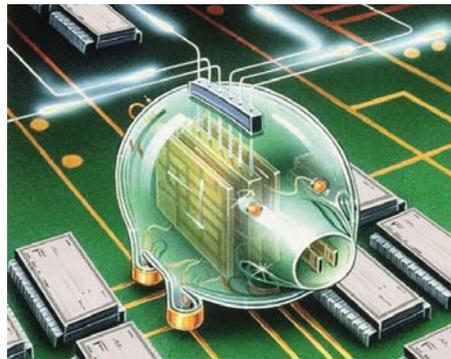
What is Check 21?

In its simplest terms, Check 21 will enable financial institutions to achieve many of the benefits of electronic processing without mandating the receipt of checks in electronic form. Under Check 21, financial institutions will be able to create substitute checks, also known as image replacement documents (IRDs). A substitute check, which can be processed just like an original check, is a paper reproduction of the original check created from a digital image. Checks can be cleared more quickly by truncating the original checks, transmitting electronic check data and images, then printing substitute checks for presentment. The substitute check, not the check image, serves as the legal equivalent of the original check.

What benefits will Check 21 bring?

- **More choices** – By taking advantage of electronic check presentment and return capabilities, financial institutions can choose an alternative to today's paper-based processing system.

- **Increased efficiencies** – By reengineering their infrastructure with electronics, institutions can expedite the collection or return of checks, streamline internal processes, reduce operating costs and realize greater efficiencies.
- **Greater innovation** – By providing innovative new services, institutions can broaden deposit options or extend deposit cutoff hours.



How will the Federal Reserve respond?

The Federal Reserve will be ready with “day one” Check 21 products when the legislation goes into effect. The Reserve Banks intend to introduce a new suite of services to offer customers more options than ever before:

- **Forward and return image cash letters** Customers with image-enabled operations will be able to send image cash letters directly to the Federal Reserve. These images can be quickly sent to the paying bank or to a Federal Reserve office for substitute check creation and physical presentment. Customers will also be able to send return image cash letters to the Federal Reserve, resulting in a more efficient process for return item pulls, return item qualification and cash letter creation.

- **Image cash letter conversion** For customers not yet image-enabled, Reserve Banks will selectively create image cash letters on their behalf to expedite clearing, reduce operating costs and extend processing windows. This will facilitate accelerated clearing of large-dollar items and improve deposit times.
- **Image cash letter delivery** Customers ready to accept image cash letters will be able to receive their Federal Reserve presentments earlier than they do today, allowing for earlier posting and new income opportunities. Image cash letter delivery will eliminate processing and storing of physical items, while supporting an on-site archive of images that can be converted to legal check documents.

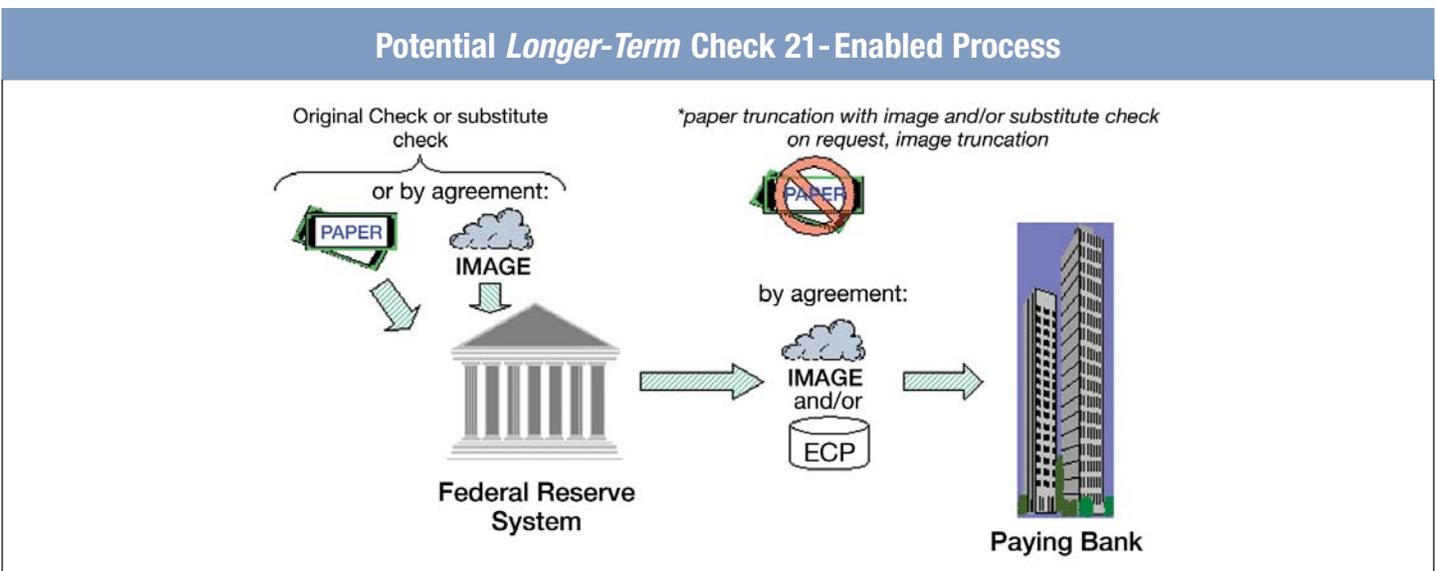
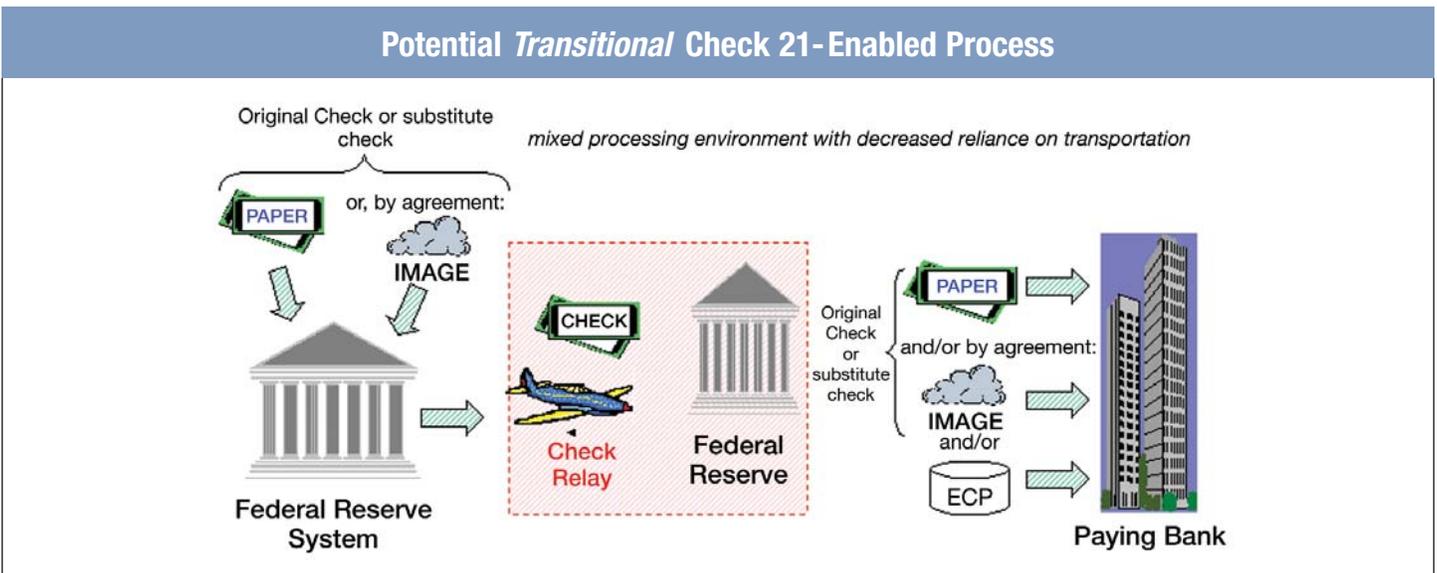
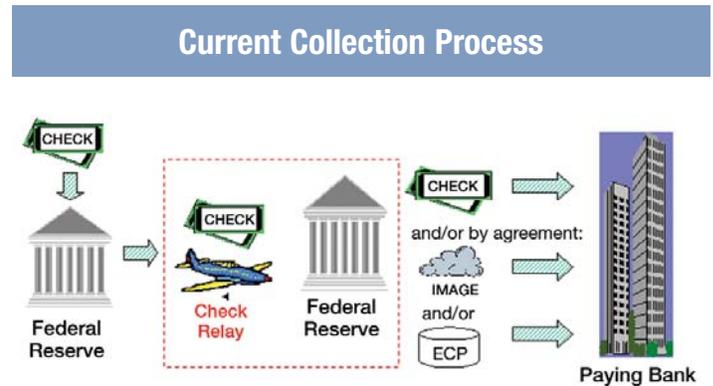
“We’re excited by the near- and long-term potential of this legislation,” says Patrick Barron, first vice president at the Federal Reserve Bank of Atlanta and director of the Retail Payments Office. “Check 21 will spur the use of new technologies today that will improve the efficiency and reduce the cost of the nation’s check collection system and provide better services to bank customers for years to come.”

Over the course of the next year, you can count on the Federal Reserve to deliver up-to-date reliable information about Check 21 to support your planning efforts. We are actively planning educational events and regular communication to keep you informed as news develops. If you have questions about Check 21 and Federal Reserve plans or need information to support your institution’s planning, please contact your account manager in Minneapolis at 1-800-553-9656 ext. 6933 or in Helena at 1-800-823-4333 ext. 3877. ☞

Check 21 – Frequently Asked Questions

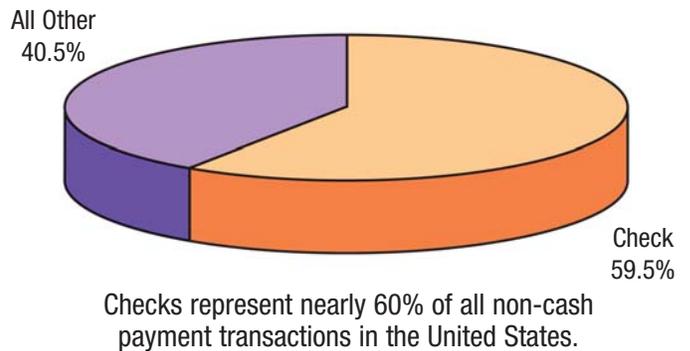
Q How will Check 21 change the way checks are processed?

A Under current law, unless an agreement is in place between financial institutions, a depository institution or its agent must present the original paper check to the paying bank. Under Check 21, the paying bank is required to accept presentment of a substitute check in place of the original check. As a result, financial institutions may choose to truncate original paper checks, process and transmit checks electronically, and have substitute checks printed at a location near the paying bank for presentment. This market-based approach permits each financial institution to decide whether to make use of this new authority to create substitute checks based on its business judgment about the costs and benefits of doing so.



Q People are writing fewer and fewer checks already, so why enact this legislation now?

A Although the overall volume of checks has declined during the past several years, about 40 billion checks continue to be written annually in the United States, and the Federal Reserve is processing 16.5 billion of those checks. It is clear that checks will not go away overnight. However, moving large volumes of paper across the country is relatively slow and expensive, and subject to the risks of weather and other factors that may hinder timely transport. Check 21 will facilitate the use of electronics where it is cost-effective to do so, thereby enhancing payment system efficiency.

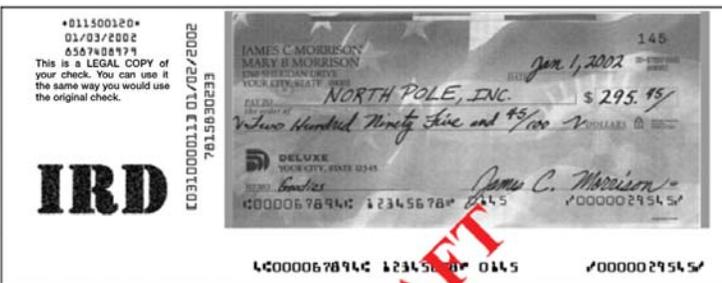


Q Will all checks be processed electronically following enactment of Check 21?

A No. The Act does not require financial institutions to accept checks in electronic form, nor does it require institutions to use the new authority granted by the Act to create substitute checks. Financial institutions may choose to exchange check information electronically, but only by agreement.

Q Are financial institutions required to establish agreements for substitute check presentment?

A No. The Act enables financial institutions to present substitute checks to one another without an agreement in place. If the substitute check meets the requirements of the Act, it becomes the legal equivalent of the original check and can be used in the same way as the original.



Q Does a substitute check need to contain an image of both the front and back of the original?

A Yes. To be the legal equivalent of the original check, the substitute check must accurately represent all of the information contained on the front and back of the original.



Substitute check design

Q Can a financial institution dishonor a substitute check simply because it wants the original check?

A No. Provided that the substitute check meets the requirements of the Act, the financial institution must accept it in place of the original.

Your Account Manager Can Help

For more information about the Federal Reserve's Check 21 plans, or to discuss opportunities that could help your institution prepare for this legislation, contact your Financial Services Account Manager. We'd be happy to answer your questions over the telephone or set up a time to meet with you.

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Additional Check 21 Resources

American Bankers Association

Federal Reserve Board of Governors

Electronic Check Clearing House Organization

Financial Services Technology Consortium

National Automated Clearing House Association

Consumers Union

www.aba.com

www.federalreserve.gov

www.eccho.org

www.fstc.org

www.nacha.org

www.consumersunion.org



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