
**THE LAW OF ELECTRONIC
FUNDS TRANSFER**

by

ROBERT C. ZIMMER

and

THERESA A. EINHORN

VOLUME I

**Card Services, Inc.
2100 Pennsylvania Avenue, N.W.
Suite 600
Washington, D.C. 20037**

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ABOUT THE AUTHORS

Robert C. Zimmer and Theresa A. Einhorn are lawyers who specialize in financial institution, commercial, corporate and antitrust law. In addition to *The Law of Electronic Funds Transfer*, Mr. Zimmer and Ms. Einhorn have published several articles regarding the financial services industry, in both legal and trade publications. They periodically address financial industry lawyers and executives on various subjects affecting both providers and consumers of financial services.

AUTHORITY OF PROVIDERS

The Comptroller's EFTS Security Guidelines suggested specific procedures designed to protect against fraud, including tampering with messages between terminals and central computer systems, unauthorized initiations of terminal transactions, fraud in connection with distribution of debit cards, unauthorized access to information and account funds by bank employees, and loss of ATM funds through burglary. The Guidelines warned national banks that security safeguards and operator procedures in terminal-based EFT systems would be reviewed during bank examination, and where evidence of "imprudent procedures" was disclosed, "corrective action would be initiated."¹⁵ The Comptroller's EFTS Consumer Guidelines, as well as the Federal Reserve Board's regulations governing consumer rights and liabilities in EFT transactions, are discussed in Chapter 5, Consumer Rights and Liabilities, *infra*.

The Office of the Comptroller of the Currency withdrew its 1976 EFTS Guidelines, in view of the fact that national banks' EFT services are subject to the comprehensive provisions of the federal EFT Act (12 U.S.C. §§ 1693-1693r) and the Federal Reserve Board's Regulation E (12 C.F.R. Part 205).¹⁶

b. Data Processing Services

The offering of EFT services has been accompanied by an expansion in the range of national banks' computer operations, and questions have been raised as to the extent to which the National Bank Act permits a national bank to provide data processing services for others. The controlling question is whether data processing activities—such as marketing excess computer time or using POS terminals and related equipment to provide information services for the merchant—constitute "incidental powers as shall be necessary to carry on the business of banking" under the National Bank Act.¹⁷

In 1984, the Office of the Comptroller of the Currency, in a revision of its 1974 ruling on data processing addressed the issue of a national banks' power to offer data processing services.¹⁸ The new ruling provides that a national bank may use data processing equipment and technology to perform for itself and others all services expressly or incidentally authorized under the laws applicable to national banks.¹⁹ The ruling sets forth the Comptroller's opinion that, in general, data processing is a technology rather than a service distinct or different from the underlying services to which it is being applied.²⁰ Thus, if the underlying service being provided by the bank

¹⁵Comptroller of the Currency, EFTS Guidelines, *supra* at 17.

¹⁶Office of the Comptroller of the Currency, Banking Bulletin No. BB-80-23 (Aug. 15, 1980).

¹⁷12 U.S.C. § 24, Seventh.

¹⁸12 C.F.R. § 7.3500.49 Fed. Reg. 11158 (March 26, 1984).

¹⁹49 Fed. Reg. 11158.

²⁰*Id.*

CONSUMER RIGHTS AND LIABILITIES

Telephone transfers are deemed to be electronic funds transfers only if they occur under a written plan or agreement between the consumer and the financial institution.¹⁹

The following transactions are excluded from the Act's definition of an electronic fund transfer:

- check guarantee or authorization "which does not directly result in a debit or credit to a consumer's account;"²⁰
- any wire transfer of funds through the Federal Reserve Communications System or similar network used primarily for transfers between financial institutions or between businesses;
- automatic transfers from a savings account to a demand deposit account to cover an overdraft or to maintain an agreed upon minimum account balance;²¹
- transfers initiated by a telephone conversation between a consumer and a financial institution employee, if the transfer is not made pursuant to a telephone bill-paying or other prearranged plan under which periodic or recurring transfers are contemplated;^{21a}
- any transfer the primary purpose of which is the purchase or sale of securities or commodities regulated by the Securities and Exchange Commission or the Commodity Futures Trading Commission.²²

¹⁹Reg. E. Commentary Q. 3-14 through 3-19.

²⁰Under the Federal Reserve Board's interpretation of the Act, "memo-posting" or putting a hold on the consumer's funds in the amount of the guaranteed or authorized check does not "directly result in a debit" to the account, and thus, check guarantee/authorization services using such holds are exempt from the Act. Reg. E Commentary Q. 3-1.

²¹Federal Reserve and FDIC regulations specifically permit such automatic transfers from savings to checking. 12 C.F.R. §§ 217.5(c)(2) (Regulation Q); 329.5(c)(2).

^{21a}In *Kashanchi v. Texas Commercial Medical Bank, N.A.*, No. 82-2242 (5th Cir. May 2, 1983), the court confirmed that the EFT Act does not govern a transfer of funds from a consumer's account that is initiated by a phone conversation (even if unauthorized) between a "consumer" and an employee of the financial institution, unless the transfer was made pursuant to a prearranged plan under which periodic transfers are contemplated. In *Kashanchi* the Plaintiff alleged that a transfer from her account was instituted by a telephone conversation between a bank employee and an unauthorized third party, and argued that the transfer was an unauthorized transfer covered by § 909 of the EFT Act, which would limit her loss to \$50 (see pp. 68-C to 68-H. *infra*). She argued that telephone transfers were excluded from EFT Act coverage only when the "consumer" was the actual accountholder from whose account the funds were transferred. The court rejected this argument and ruled that it was clear from the plain language of the Act that "consumer" was intended to cover all natural persons, not just specific accountholders.

²²EFT Act § 903(6); 12 C.F.R. § 205.3. The Federal Reserve Board has explained that under arrangements by which a consumer uses a debit card to purchase goods or services and funds are automatically transferred by a broker from a money market fund to the card issuer for payment, the transfer would not be exempt since its primary purpose was not the purchase or sale of securities. Reg. E Commentary Q. 3-3.5.

CONSUMER RIGHTS AND LIABILITIES

correspondent bank, which sends a computer print-out listing the payees and the payment amounts, together with a composite check payable to the financial institution. These transfers are subject to the Act because they are initiated by electronic means. (Q. 2-18)

- A creditor obtains authorization from consumers to debit their accounts periodically, and the financial institution debits the consumers' accounts in accordance with billing information contained on magnetic tape provided by the payee, and sends the payee a composite check.—These transfers are subject to the Act, because they are initiated by electronic means. (Q. 2-19)
- A consumer authorizes a company to debit an account automatically for a payment, and the company presents a paper draft that ultimately is debited against the consumer's account at the financial institution.—The transfer is not subject to the Act, because it is initiated by a paper draft. It would be an electronic fund transfer subject to the Act, however, if the transfer were via an ACH. (Q. 2-20)
- A consumer authorizes the financial institution to make recurring payments to another party from the consumer's account, or to make recurring interest payments to the consumer, and the institution periodically generates an individual check to the payee by computer.—No "electronic fund transfer" is involved, because the transfers are initiated by check (even though the check is computer-generated). (Q. 2-21)

In some cases, significant operational difficulties have arisen from the application of the EFT Act and Reg. E to certain types of transactions. For example, the Federal Reserve Board found it necessary to grant a special exemption from the Act's receipt requirement for home banking services.²⁴ Section 906 of the EFT Act requires that a receipt be made available to the consumer for all transfers initiated at an electronic terminal. Although the Act exempts telephones from the definition of a "terminal," no similar exemption was made by Congress for home terminals.

The receipt requirement threatened to render even experimental home banking services prohibitively expensive, and would have required that a printer be placed in the consumer's home. The Federal Reserve Board staff, recognizing this problem, granted a limited exemption for home banking terminals under the EFT Act and Reg. E. The Board's staff explains in its official Reg. E commentary that home terminals are analogous to telephones in function, and therefore should be given a similar exemption. The relevant portion of the staff commentary provides as follows:

2-23 Q: Home terminals. Some financial institutions offer home banking services to their customers. The service will typically involve the use, for example, of a home computer terminal or a television set that is

²⁴Reg. E Commentary Q. 2-23.

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