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Melvin R. Katskee

Ann L. Wright

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An Overview of the Legal Issues Confronting the Establishment of Electronic Funds Transfer Services[†]

by MELVIN R. KATSKEE* & ANN L. WRIGHT**

INTRODUCTION

The electronic funds transfer revolution has burst like a thunderclap over the banking and legal communities. Spurred by the pressures of the paper-based check system, which has been found to be a costly, time-consuming and inconvenient payment mechanism,¹ financial institutions have sought out and experimented with various electronic means of expanding and speeding up a customer's accessibility to his accounts. Computer technology has been utilized to promote this accessibility.²

Essentially, electronic funds transfer is a process of value exchange achieved through the use of electronic devices. The value exchange is brought about by debit or credit orders. The transfer of funds at various institutions is initiated through an electronic in-

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* A.B. cum laude 1967, Creighton University, Omaha, Nebraska; J.D. 1970, Univ. of Nebraska, Lincoln, Nebraska. Mr. Katskee is a member of the Nebraska State Bar Ass'n, Second vice-president and general attorney, The Omaha Nat'l Bank, and formerly adjunct professor of law, Creighton Univ. School of Law, Omaha, Nebraska.

** J.D. 1979, Creighton Univ. School of Law, Omaha, Nebraska. Ms. Wright is currently serving in the Army Judge Advocate General's Corp.

1. Brace, *Electronic Funds Transfer System: Legal Perspectives*, 14 OSGOODE HALL L.J. 787, 787 (1976); Feldman, *Consumer Industry Issues Involved in EFTS*, in PLI, ELECTRONIC FUNDS TRANSFER 165, 168 (1977) [hereinafter PLI].

2. "A half-way step in the conversion from paper to electronics is truncation, which stops the paper collection process at an early stage. The bank credit card industry is increasingly engaging in that truncation process today and will cease interchanging paper by mid-1977." Brandel, *Electronic Funds Transfer: Commercial and Consumer Law Aspects*, 17 JURIMETRICS J. 201 (1977), reprinted in 82 COM. L.J. 78 (1977) & PLI, *supra* note 1, at 253, 256-57.

terfacing process between the separate facilities.³ Several primary types of systems are generally encompassed within the term electronic funds transfer.⁴

The automated clearing house (ACH)⁵ was the first system to be put into actual operation. This system is not one designed for direct use by the public, but rather is a computerized, inter-bank transfer system. Through the system an originating bank can transfer payments electronically or via computer tapes to the automated clearing house; once the message reaches the clearing house, it may then be changed into another medium for transfer to the customer's bank of deposit. The ACH is used for direct deposit of payroll or government benefit payments, for preauthorized debits such as recurring monthly bills, and for other transactions which transfer funds from one financial institution to another.

Another electronic funds transfer device is the automatic teller machine (ATM)⁶ —an unmanned system that takes deposits, disburses cash and transfers funds from one account to another without processing paper for collection. The remote, manned teller is basically an ATM which is operated for the customer by a person who may or may not be an employee of the customer's financial institution.

A third device is the point-of-sale system (POS),⁷ which simul-

3. See B. CLARK, *THE LAW OF BANK DEPOSITS, COLLECTIONS, AND CREDIT CARDS* 187 (1976 Cum. Supp.).

4. NATIONAL COMM'N ON ELECTRONIC FUND TRANSFERS, *EFT AND THE PUBLIC INTEREST* 1 n.1 (1977).

5. ACH is defined as a "computerized facility used by member depository institutions to process, i.e., combine, sort and distribute payment orders in machine-readable form (computer tapes or punched cards)." NAT'L SCIENCE FOUNDATION, *THE CONSEQUENCES OF ELECTRONIC FUNDS TRANSFER* 239 (1975) (report by Arthur D. Little, Inc.) [hereinafter cited as NSF REPORT]. See also PEAT, MARWICK, MITCHELL & CO., *EFT: A STRATEGY PERSPECTIVE* 7 (1977).

6. The ATM is defined as a "machine capable of processing a variety of transactions between a depository institution and its customers. These functions might include accepting deposits, providing withdrawals, transferring funds between accounts, and accepting instructions to pay third parties to the transaction. An automated teller machine may or may not be on-line to a computer system and may be placed on or off the premises of a depository institution. Placement in certain locations may permit customer access seven days a week, 24 hours a day." NSF REPORT, *supra* note 5, at 239. The ATM typically consists, from the customer's viewpoint, of a keyboard which is used to instruct the machine, slots for inserting an identification card and deposits, and a slot from which packets of cash emerge. See, e.g., *Colorado ex rel. State Banking Bd. v. First Nat'l Bank*, 394 F. Supp. 979, 981-82 (D. Colo. 1975), *aff'd in part and rev'd in part*, 540 F.2d 497 (10th Cir. 1976), *cert. denied*, 429 U.S. 1097 (1977).

7. The POS system is defined as a "communication and data capture terminal located where goods or services are paid for. POS terminals may serve merchant ac-

taneously debits the customer's account and credits the merchant's account for the payment of goods or services. Other possible features of a POS system include check verification, where the bank replaces the consumer's obligation to a merchant with its own by electronically guaranteeing payment of the check, credit authorization, and credit card or cash transactions.⁸ Currently, most POS facilities are used for verification services only.

EFT, in its broader meaning and as used in several statutes, also encompasses pay-by-phone transactions and inter-account transfers, which provide for the accrual of interest on sums that are, in effect, available on demand.

This article will consider some of the basic legal issues with which legislatures must deal in enacting EFT legislation and which courts must address in resolving disputes. These issues include the applicability of non-EFT banking laws to terminals and businesses involved in providing EFT services; the effect of antitrust laws on facility ownership and use; the protection for consumers of EFT; and the protection for the privacy of EFT account holders.

I. NON-EFT BANKING LAWS AND THEIR APPLICABILITY

One of the first cases which dealt with an electronic funds transfer system addressed the question of whether the merchant running the terminal, who cashed a consumer's check in part by authorizing a bank transfer from its deposit account to that of the consumer, was accepting deposits, and thus, engaging in the business of banking. In *Nebraska ex rel. Meyer v. American Community Stores Corp.*,⁹ the system in issue was one which permitted the customer of a savings and loan institution to gain access to his account to make deposits, withdrawals or transfers of funds at the supermarket, through the use of an encoded card. The supermarket's employees handled all of the transactions.¹⁰

counting needs and may assist in processing financial transactions. In the latter case, the terminal may operate as part of an authorization/verification system or initiate direct exchanges of value among merchants, customers and financial institutions." NSF REPORT, *supra* note 5, at 244. See *Hearings On Electronic Funds Transfer Systems and the Failure of the U.S. Nat'l Bank of San Diego Before the Subcomm. on Bank Supervision and Insurance of the House Comm. on Banking and Currency*, 93rd Cong., 1st Sess. 28 (1973).

8. Note, *Electronic Funds Transfer Systems: A Need for New Law?*, 12 NEW ENG. L. REV. 111 (1976); Fried, *Electronic Funds Transfer*, ANN. SURVEY AM. L. 23 (1976).

9. 193 Neb. 634, 228 N.W.2d 299 (1975).

10. If a customer wishes to deposit in his or her First Federal account, the customer goes to the courtesy counter of the store and obtains a transaction slip from a store employee. When that slip is filled out, the respondent's employee then places the two electronically embossed and coded TMS cards in

The terminal had been established under a Federal Home Loan Bank Board (FHLBB) regulation authorizing savings and loans to use "remote service units" (functionally equivalent to ATMs).¹¹ That regulation was the first to allow deployment of EFT by federally regulated financial institutions,¹² and the EFT system involved was the pilot project for terminal deployment.

The State contended that the use of an on-line terminal for these transactions constituted unlawful engagement in the banking or savings and loan business. The Nebraska supreme court rejected that argument, holding in part that the arrangement did not violate state banking law restrictions, since no debtor-creditor contractual relationship arose between the store and the customer. In the court's view, the store was simply the financial and operational intermediary between the depositor and the savings and loan, since the evidence showed that the store did "not accept or retain deposits, nor promise to repay them or return them to anyone."¹³

The issue of whether or not merchants who provided room for terminals should be subject to banking laws and regulations arose again when the states began enacting EFT deployment legislation. Large chain stores lobbied to prevent state financial institution regulators from having control over their businesses.¹⁴ As a result, many state statutes speak to the duties of the financial institutions and the rights of the account holders, leaving the merchants who provide

the terminal. One card identifies the store and the other identifies the customer. The customer also has to furnish certain personal confidential numbers, which are not contained on the card, for the purpose of verifying that the person using the card is authorized to use it. The store employee then uses the telephone on the terminal to activate the on-line computer, which is located at the main office of First Federal. The computer then verifies the account and the information. Once verification has been made, the transaction proceeds instantaneously. The computer debits the store's account at First Federal in the amount of the customer's deposit; credits the customer's account at First Federal in the same amount; and notifies the terminal operator that the transaction has been completed. The store then accepts from the customer the money or check representing the deposit and the money is placed in the cash register with other money of the store.

In the case of a withdrawal the procedure is essentially the same except that in this case the computer debits the customer's First Federal account and credits the store's First Federal account, and the store then pays the amount of the withdrawal in cash to the customer from the store's cash drawer.

Id. at 636-37, 228 N.W.2d at 301.

11. 12 C.F.R. § 545.4-2 (1979).

12. See Greguras, *Electronic Funds Transfers and the Financial Institution/Consumer Relationship*, 10 U.C.C.L.J. 172, 176 (1978).

13. 193 Neb. at 640, 228 N.W.2d at 302-03.

14. See, e.g., Testimony of Lynn J. Ellins, midwest regional counsel, J.C. Penney Co., to the Ill. Elec. Fund Transfer Sys. Study Comm'n, Oct. 30, 1977, reprinted in PLI, *ELECTRONIC FUNDS TRANSFER* 207 (1978).

space for terminals completely out of the statutory scheme of rights and liabilities.¹⁵ Other statutes allow the regulators to oversee only the terminal business in the retail store and limit the store's actions only by restricting the release of account information for privacy protection.¹⁶

The most important banking law issue to arise in the EFT context is the effect of the federal laws regulating branch banking on off-premises terminal deployment. The basic federal branch banking law is contained in the McFadden Act, as amended in 1933,¹⁷ which states that "[t]he term 'branch' as used in this section shall be held to include any branch bank, branch office, branch agency, additional office, or any branch place of business . . . at which deposits are received, or checks paid, or money lent."¹⁸ Section 36(c) of the McFadden Act provides that a national bank may:

with the approval of the Comptroller of the Currency, establish and operate new branches: (1) Within the limits of the city, . . . in which said association is situated, if such establishment and operation are at the time expressly authorized to State banks by the law of the State in question; and (2) at any point within the State in which said association is situated, if such establishment and operation are at the time authorized to State banks by the statute law of the State in question by language specifically granting such authority. . . .¹⁹

The United States Supreme Court has interpreted these statutory sections in two major cases. In *First National Bank of Logan, Utah v. Walker Bank & Trust Co.*,²⁰ two national banks with their main facilities in Logan and Ogden, Utah, respectively, sought to open branches. Both national banks attempted to establish these branches without complying with the Utah law on branching. Both banks relied upon the provisions of the McFadden Act, and the approval of the Comptroller of the Currency.²¹

Suits were filed in two different district courts contesting the action of the banks. In one case, the Utah federal district court upheld the bank's action, noting that there was no requirement in the fed-

15. See, e.g., COLO. REV. STAT. §§ 11-6.5-101 *et seq.* (1977); FLA. STAT. § 65g.062 (1975); 1977 N.M. Laws, ch. 359.

16. See, e.g., IOWA CODE § 527.3 (1978).

17. 12 U.S.C. § 36(f) (1976).

18. *Id.*

19. *Id.* § 36(c). These restrictions apply only to banks. Federally chartered savings and loans are not restricted as to branching or locations of remote service units. See 12 C.F.R., Part 545 (1979).

20. 385 U.S. 252 (1966).

21. *Id.* at 255.

eral statute that national banks comply with all state conditions.²² On appeal, the United States Court of Appeals for the Tenth Circuit reversed,²³ stating that section 36(c)(1) of the Act "acceded to state law and . . . intended to create and maintain a competitive equality between state and national banks."²⁴

In the second case, the district court for the District of Columbia, granting the injunctive relief sought, held that the Utah laws restricted the activities of national banks.²⁵ The District of Columbia Court of Appeals affirmed without opinion, citing the case from the Tenth Circuit. Due to a conflict between these opinions and a related fourth circuit case,²⁶ *certiorari* was granted by the United States Supreme Court.

The Supreme Court first traced the legislative history of the section, which was part of the Banking Act of 1933, an amendment to the McFadden Act of 1927.²⁷ The opinion stressed that the original attempt to permit branches without reference to state law, as advocated by the Comptroller, had suffered defeat in the seventy-first Congress.²⁸ Eventually, Section 36(c) was enacted as a part of the Banking Act of 1933. The opinion made copious reference to floor debates.²⁹ From this recital of legislative history, Justice Clark had no difficulty in finding that the Utah restrictions were absorbed into the provisions of sections 36(c)(1) and (2), and that national banks were therefore subject to state branching laws.³⁰

The second important case was *First National Bank in Plant City v. Dickinson*.³¹ In *Plant City*, the bank had established an ar-

22. Walker Bank & Trust Co. v. Saxon, 234 F. Supp. 74, 77-79 (D. Utah 1964).

23. Walker Bank & Trust Co. v. Saxon, 352 F.2d 90 (10th Cir. 1965).

24. *Id.* at 94.

25. Commercial Security Bank v. Saxon, 236 F. Supp. 457 (D.D.C. 1964).

26. First Nat'l Bank of Smithfield v. Saxon, 352 F.2d 267 (4th Cir. 1965).

27. 385 U.S. 252, 256-60 (1966).

28. *Id.* at 259.

29. In a colloquy on the floor of the Senate with Senator Copeland as to the purpose of the Act (with reference to branch banking by national banks), Senator Glass said that it would be permissible "in only those States the laws of which permit branch banking, and only to the extent that the State laws permit branch banking." Moreover, to make it crystal clear, . . . Senator Glass was careful to repeat: "*Only in those States and to the extent that the State laws permit branch banking.*" (Emphasis added.) 76 Cong. Rec. 2511 (1933). Remarks of other members of Congress also indicate that they shared the understanding of Senator Glass. For example, Senator Vandenberg stated that 36(c)(1) provides "that the branch banking privilege so far as national banks are concerned shall follow the status established by State law in respect to the State privilege." 76 Cong. Rec. 2262 (1933).

Id. at 259.

30. *Id.* at 261; citations omitted.

31. 396 U.S. 122 (1969).

more car service pursuant to a Comptroller of the Currency regulation,³² which stated that deposits collected by the armored car, pursuant to an agreement with the customer which specified that the messenger was the agent of the customer, were not to be deemed to have been received by the bank until delivered to the bank premises. The Florida State Comptroller advised the bank that the service violated Florida branch banking prohibitions³³ and the bank sued for a declaratory judgment.

Chief Justice Burger, author of the majority opinion, determined that the federal definition of branch banking prevailed,³⁴ and that state law only came into play to determine where and when branch banks might be operated.³⁵ The Chief Justice gave the federal law definition a liberal interpretation in order to promote what he found was the congressional "policy of competitive equality."³⁶ Analyzing the definition of "branch" found in section 36(f), the Chief Justice noted that the term was defined as "any branch bank, branch office, branch agency, additional office, or any branch place of business . . . at which deposits are received, or checks paid or money lent."³⁷ He observed that the definition was in the disjunctive, and that the offering of any one or more of the three services provided a sufficient basis for a finding that branch banking was taking place.³⁸ The Court ignored the contractual provision between the bank and the customer³⁹ and held that "deposits" were in fact received by the bank away from its chartered premises, providing the bank a competitive advantage not shared by state banks.⁴⁰

Despite the obstacles presented by these authoritative, but much criticized, Supreme Court opinions,⁴¹ the Comptroller of the

32. Comptroller's Manual for National Banks ¶7490, *quoted in* 396 U.S. at 126-28 n.2.

33. FLA. STAT. § 659.06(1)(a) (1965).

34. 396 U.S. 122, 133-34 (1969).

35. *Id.*

36. *Id.* at 133.

37. *Id.* at 134.

38. *Id.* at 135.

39. *Id.* at 136-37.

40. *Id.* at 137-38.

41. See Katskee, *The Assault Upon the Armored Car—The Branch Banking Bête Noire*, 91 BANKING L.J. 962 (1974); W. BAXTER, P. COOTNER & K. SCOTT, *RETAIL BANKING IN THE ELECTRONIC AGE—THE LAW AND ECONOMICS OF ELECTRONIC FUNDS TRANSFER* (1977) [hereinafter cited as BAXTER], where the authors state:

Thus, the Supreme Court in *Plant City* ignored the history of branching and the consequences of its interpretation in order to define the reach of Section 36 and the concept of a branch in the light of an assumed Congressional objective of competitive equality—an objective of limited validity when employed within the scope of Section 36 and of total inappropriateness when employed to ascertain the section's boundaries. A decision of this sort—un-

Currency, in December 1974, promulgated an interpretation which permitted national banks to install and operate customer-bank communication terminals (CBCTs).⁴² The Comptroller held that CBCTs were not branches, and therefore, not subject to the limitations of section 36(c).⁴³ This position was adopted to allow national banks to maintain competitive equality with federal savings and loans, which were permitted to deploy EFT terminals on a relatively unregulated basis.⁴⁴

According to the Comptroller, CBCTs could be free-standing or located in a business establishment, manned or unmanned, on-line or off-line.⁴⁵ These CBCTs could be used to effect cash withdrawals from an account or from a pre-arranged line of credit, make deposits to an account, initiate inter-account transfers or transfer funds from the account of one customer to another customer.⁴⁶ Only existing customers of the bank could avail themselves of the services of the CBCTs, and no loans could be made unless against a pre-arranged line of credit.⁴⁷

Following public hearings, the Comptroller amended his original interpretation to limit placement of CBCTs to an area no further than fifty miles from the main office or any branch office of the bank, except for CBCTs shared with other financial institutions and POS terminals through which cash was not dispensed and deposits were not accepted.⁴⁸

The reaction to the Comptroller's interpretation was a multitude of lawsuits.⁴⁹ In general, the courts rejected the Comptroller's interpretation, at least in part. Finally, in *Independent Bankers Associa-*

sound in some fundamental respects but nonetheless authoritative—creates a dilemma for lower courts. They can faithfully carry out and extend the reasoning and premises of the Supreme Court's opinion. Or, as its shortcomings become apparent, they can strive to limit its reach as much as possible. . . .

Id. at 124-25.

42. 12 C.F.R. § 7.7491 (1974).

43. *Id.*

44. *Id.*

45. *Id.* The term "on line" means that the EFT terminal is directly connected by wire to the central accounts computer at the main bank office. NSF REPORT, *supra* note 5, at 244. For a technical discussion of this process, see generally 2 MID-AMERICA PAYMENTS STUDY REPORT, SYSTEM DESIGN SPECIFICATIONS 102-16 (1975).

46. 12 C.F.R. § 7.7491 (1974).

47. *Id.*

48. 40 Fed. Reg. 21,703 (1975).

49. See Peck & McMahon, *Recent Federal Litigation Relating to Customer-Bank Communication Terminals ("CBCTs") and the McFadden Act*, 32 BUS. LAW. 1657 (1977); Traeger & Peck, *EFTS Litigation*, in PLI, *supra* note 1, at 19, 26-32; BAXTER, *supra* note 41, at 121-28; Note, *Customer-Bank Communication Terminals and the McFadden Act Definition of a "Branch Bank,"* 42 U. CHI. L. REV. 362 (1975).

tion of America v. Smith,⁵⁰ the court directly held that CBCTs transact business which is also carried on at main banking offices, and are therefore branches within the meaning of section 36(f).⁵¹ The "competitive equality" theory developed in the *Logan* and *Plant City* cases was stressed.⁵² Following that decision, the Comptroller withdrew his CBCT interpretation and, on November 3, 1976, published an altered regulation which allowed national banks to establish a new type of branch that (1) could be shared with other banks, (2) had special capital requirements of a lesser nature than regular branches, and (3) was not subject to the bulk of supplemental application procedures required for ordinary branches.⁵³ The Comptroller thus concluded that EFT facilities are branches, but sought to avoid the capital requirements of "brick and mortar" branches for remote terminals.

It has been suggested that the broad interpretation of the definition of a "branch," as well as the theory of competitive equality, were new substantive policies developed by the Supreme Court.⁵⁴ If competitive equality is indeed the objective of federal law, national banks in some twenty-one states where state law has defined CBCTs as not constituting branches must meet federal, and possibly even state, branching capital requirements not equally imposed upon state banks. If national banks are to have an equal opportunity to utilize technological developments, Congress must act directly by passing EFT deployment legislation and clarifying the role of state law in national bank operations.

There remains a method that can be used by a national bank desiring to take advantage of the electronic funds transfer technology without "eating the bitter fruit" of the *Plant City* decision. This method centers around the limiting language in the *Smith* and other case decisions, that off-premises CBCTs are branches if the devices

50. 534 F.2d 921 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 862 (1976).

51. *Id.* at 930.

52. *Id.* at 932-37.

53. 41 Fed. Reg. 36,198 (1976); 41 Fed. Reg. 48,333 (1976). The rule changes include procedures regarding applications by national banks to establish CBCT terminals. Section 4.5a was added to Title 12, directing national banks to submit applications for CBCT branches to the Regional Administrator. Section 5.1 was also revised to direct that CBCT applications are not subject to the application provisions of Part 5 except for specific CBCT notice publication provisions set out in 12 C.F.R. § 5.2a. Section 8.3 was amended to provide a CBCT application fee of \$200.

54. See D. Prives, E.F.T. Policy and Competitive Equality: The Roles of Courts and Congress 21-25 (Harv. U. Prog. on Information Tech. & Public Policy, Pub. No. P-77-1, Jan. 1977).

are owned, rented, established or provided by a national bank.⁵⁵ The possibility exists that an electronic funds transfer network owned and operated by others, and servicing a national bank as an independent contractor, could escape altogether the branching restrictions of federal law.⁵⁶ These third parties, however, could still be attacked for unlawfully engaging in the banking business.⁵⁷

Looking to branching requirements for the authority to deploy EFT terminals only creates legal and practical confusion. Several states have already recognized the unique nature of these new services by enacting separate EFT deployment legislation.⁵⁸ Congress, however, has thus far failed to provide such a direct solution.

One court has taken a different approach on this issue. On April 20, 1979, the Court of Appeals for the District of Columbia "pulled the rug" out from under federally regulated, financial institutions which provided certain types of EFT services. In *American Bankers Association v. Connell*⁵⁹ and two companion cases, the appellate court ruled that there is no statutory authority for regulations which allow the use of "automatic fund transfers" by commercial banks, "remote service units" by savings and loan associations, and "share drafts" by federal credit unions.⁶⁰ The court found that these devices blur the statutory distinction between the different types of financial institutions by improperly allowing interest on demand (checking) accounts at commercial banks and by permitting savings and loans and credit unions to provide services in the nature of interest-bearing checking accounts.⁶¹ The court set aside the regulations authorizing such services for federally regulated financial institutions, effective January 1, 1980.⁶² The court urged Congress to act before that time to either establish a new statutory policy as to the electronic devices and the functions of the different financial institutions or purposely to retain the present law forbidding use of these new technologies.⁶³

55. See, e.g., *Independent Bankers Ass'n v. Smith*, 534 F. 2d 921, 951 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 862 (1976).

56. Peck & McMahon, *supra* note 49, at 1681-83; BAXTER, *supra* note 41, at 132.

57. See text accompanying notes 9-13 *supra*.

58. See, e.g., COLO. REV. STAT. §§ 11-6.5-103(6), 11-48-103 (1977); MINN. STAT. §§ 47.62 (1), 47.65 (1978); N.M. LAWS §§ 58-16-5, 58-16-6 & 58-16-10 (1978).

59. FED. BANKING L. REP. (CCH) ¶ 97,785 at 83,547 (D.C. Cir. 1979).

60. *Id.*

61. *Id.* at 83.

62. *Id.* The affected regulations are 43 Fed. Reg. 20,001 (1978) (Federal Reserve System) 43 Fed. Reg. 20,222 (1978) (Federal Deposit Insurance Corporation), 12 C.F.R. § 545.4-2 (1978) (Federal Home Loan Bank Board) and 12 C.F.R. § 701.34 (1978) (National Credit Union Administration).

63. FED. BANKING L. REP. (CCH) ¶ 97,785, at 83,547, 83,548 (D.C. Cir. 1979).

In response to the *Connell* decision, on May 1, 1979, Representative St. Germain of Rhode Island introduced the Consumer Checking Account Equity Act of 1979.⁶⁴ This bill would authorize the payment of interest on demand accounts and allow federally insured savings and loan associations and credit unions to offer demand accounts.

President Carter has also proposed to Congress that the ceilings on interest-bearing accounts at all federally regulated financial institutions be lifted and that interest-bearing demand accounts be authorized for all federally insured banks, savings and loans and mutual savings banks.⁶⁵

Although these congressional and presidential proposals would not clearly define the extent to which EFT services may be offered by national financial institutions, they would remove the basis for the objections of the *Connell* court relating to interest on demand accounts and demand accounts by thrift institutions. This would at least prevent suspension of many services at the beginning of 1980.

II. SHARING AND THE ANTITRUST LAWS

Apart from the issues of branch banking and its effect on electronic funds transfer systems, but of equal importance, are various antitrust considerations that must be addressed in the EFT context.⁶⁶ To some extent these antitrust issues have been highlighted by laws passed in various states which authorize the establishment of EFT systems, but require financial institutions establishing such systems to share such facilities with all, or certain other, financial institutions.⁶⁷ Justice Department statements in recent years,⁶⁸ though fragmented, do provide guidance for financial institutions desiring to engage in cooperative EFT activities. Such activities may take the form of common standards, joint ownership of central switching facilities, access to supporting communication lines, or the ownership and use of remote terminals.

64. H.R. 3864, 96th Cong., 1st Sess. (1979).

65. *Carter Calls for End to Federal Controls on Interest Rates, Citing Inflation Impact*, Wall St. J., May 23, 1979, at 3, col. 2.

66. See generally Murray, *EFTS and Anti-Trust—Some Reflections on the Possibilities*, 37 U. PITT. L. REV. 673 (1976); Ubell, *Electronic Funds Transfer and Antitrust Laws*, 93 BANKING L.J. 43 (1976); Horodas, *Ownership and Control of Electronic Funds Transfer Systems in the United States*, 1 COMPUTER/L.J. 501, 510-15 (1979).

67. See, e.g., IOWA CODE § 527.5 (1976). Joint activities are tested by their "tendency" toward monopoly or their "reasonable likelihood" of substantial lessening of competition in the market. *United States v. Penn-Olin Chem. Co.*, 378 U.S. 158 (1964); Ubell, *supra* note 66, at 73-79.

68. See note 75 *infra*. See also Baker, *Antitrust and Automated Banking*, 90 BANKING L.J. 703 (1973).

As a general rule, joint activities must be limited to those necessary to accomplish the legitimate functions of the joint venture.⁶⁹ Moreover, the activities must be free of anti-competitive characteristics, such as price-fixing, production control,⁷⁰ group boycotts,⁷¹ tying arrangements,⁷² and certain agreements to limit distribution.⁷³ The position of the Justice Department relative to mandatory sharing laws is that such laws do not invoke any antitrust exception.⁷⁴ The activities of sharing institutions must, therefore, be justified on the same basis as any other joint venture or sharing arrangement.

That the Justice Department is in earnest was reflected by its announcement of antitrust objections to a proposed joint venture of commercial banks in Nebraska that sought to develop a shared EFT system. The Justice Department opposed the joint venture because the mandatory sharing provisions of the Nebraska law tended to "undercut incentives to innovate and to create a 'free rider' problem with respect to those who join the system after it starts operating and thus avoid the initial risk taking."⁷⁵

At about the same time that the Nebraska plan was being attacked as "overly broad,"⁷⁶ the Justice Department brought suit against the Rocky Mountain Automated Clearing House Association for being too restrictive in its membership.⁷⁷ It charged that the Association's restrictions on thrift institution membership violated the Sherman Act by creating a "combination and conspiracy in unreasonable restraint of trade and commerce."⁷⁸ These restrictions allegedly prevented the thrift institutions from competing with ACH members in offering EFT services to their customers.⁷⁹ The case was voluntarily dismissed when the ACH association opened its

69. Both horizontal agreements among competitors and vertical agreements between suppliers and dealers have been held to violate section 1 of the Sherman Act. 15 U.S.C. §§ 1-7 (1976). *Plymouth Dealer's Ass'n v. United States*, 279 F.2d 128 (9th Cir. 1960) (horizontal); *United States v. Parke Davis & Co.*, 362 U.S. 29 (1960) (vertical).

70. *Nat'l Macaroni Mfgs. Ass'n v. F.T.C.*, 345 F.2d 421 (7th Cir. 1964).

71. *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207, 212 (1959).

72. *International Salt Co. v. United States*, 332 U.S. 392, 396 (1947).

73. *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1965).

74. See note 75 *infra*.

75. Letter of Donald I. Baker, United States Dep't of Justice, to Nebraska Electronic Transfer Systems, Inc. (Mar. 1977).

76. *Justice Dept. Sees No Significant Antitrust Problem in Shared EFT*, Am. Banker, Sept. 8, 1977, at 4, col. 3.

77. See *United States v. Rocky Mountain Automated Clearing House Ass'n*, FED. BANKING L. REP. (CCH) ¶ 97,124, at 82,404 (D. Colo. 1977).

78. *Id.*

79. *Id.*

membership to all financial institutions.⁸⁰

The Nebraska and Colorado actions illustrate the thin line that the Justice Department seems to have drawn between unlawfully restrictive joint ventures designed for competitive advantage and unlawfully overbroad joint ventures which tend to discourage competition. The Justice Department has said that it sees sharing as no great problem and actively supports projects allowing for "voluntary sharing."⁸¹ It remains to be seen, however, how readily the systems in progress and being planned can meet the approved middle ground of voluntary sharing.

The antitrust implications of electronic funds transfer will be a burgeoning area as the technology and its use become more widespread. The major areas on which the antitrust laws will have an impact concern joint ventures and state mandatory sharing laws. There remains a serious question of whether state mandatory sharing laws are applicable to national banks in the absence of congressional action making them so.⁸²

III. PROTECTION FOR CONSUMERS OF EFT

The electronic funds transfer area is fraught with a wide array of consumer issues. The problems broadly concern the control, accuracy and verification of financial records, the loss of "float," whether the consumer has a stop-payment right, the extent of liability for unauthorized use of the transaction card, the right to receipts and periodic statements of account, the rights of the consumer against the seller of goods, and the types of disclosure to which the consumer is entitled.⁸³

Many of these consumer problems have been resolved by the recently enacted Financial Institutions Regulatory and Interest Rate Control Act of 1978,⁸⁴ the last section of which is the Electronic Fund Transfer Act.⁸⁵ This law was enacted on November 10, 1978,

80. *Id.*

81. See note 76 *supra*.

82. See Zimmer, *EFT and Antitrust Policy*, in PLI, *supra* note 1, at 279. On the possible inapplicability of state compulsory sharing laws, note that 12 U.S.C. § 36 (1976) does not delegate this authority to the states. Does the presence of a state EFT act relieve federally regulated financial institutions of the duty to comply with the state's branching laws? If so, the mandatory sharing laws may be applicable to those financial institutions.

83. See, e.g., Feldman, *Electronic Funds Transfers: Consumer Law Implications*, in PLI, *supra* note 1, at 209; Feldman, *Consumer and Industry Issues Involved in EFTS*, in *id.* at 165.

84. Pub. L. 95-630 (1978).

85. 15 U.S.C. §§ 1693 *et seq.* (1976) reprinted in the Appendix in this issue. [hereinafter cited as EFT Act]. The Federal Reserve Board is currently in the process of

and the provisions of the EFT Act take effect on May 10, 1980, except for the provisions on card issuance and consumer liability which are already in effect.⁸⁶ The law is applicable to both federal and state financial institutions, but preempts state law only to the extent that a state's EFT law provides less consumer protection.⁸⁷

The distribution of unsolicited EFT account access cards is limited under the Act; they may be mailed out, but may not be activated, except upon specific request.⁸⁸ The Act also provides that the terms and conditions of EFT transactions must be disclosed to account holding consumers at least once each calendar year.⁸⁹ The types of disclosures that must be provided include: the extent of the consumer's liability for unauthorized transfers; the types of transactions which may be initiated; service or other charges; the right and procedure to initiate stop payment orders for preauthorized payments; the right to receive receipts and periodic account statements; the error resolution procedure; the financial institution's liability under the law for account losses; the circumstances under which consumer account information will, in the ordinary course of business, be released to third parties; and, whether positive or negative notice of the transaction will be given in the case of preauthorized credit to the consumer's account.⁹⁰

A receipt, which provides the consumer with evidence of the transfer, is required by the Act.⁹¹ The receipt must state the type, amount and date of the transaction; the consumer's account from which or to which the funds are being transferred; the identity of any third party from whom or to whom funds are transferred; and the location or identity of the terminal making the transaction.⁹² This receipt provides the consumer with the functional equivalent of a cancelled check by which to prove payment or the occurrence of an EFT transaction.

A periodic statement, which describes each transfer, must be

promulgating regulations to implement the EFT Act. They will be codified as Regulation E, 12 C.F.R., Part 205, *reprinted in* the Appendix in this issue. Proposed regulations have been published. See 43 Fed. Reg. 60,933 (1978); 44 Fed. Reg. 18,514 (1978); 44 Fed. Reg. 25,850 (1978); 44 Fed. Reg. 30,690 (1978). The final regulations for section 909 of the EFT Act (15 U.S.C. § 1693q (1978)) were published in 44 Fed. Reg. 18,468 (1978).

86. See generally Greguras & Wright, *How the New EFT Act Affects the Financial Institution/Consumer Relationship*, 11 U.C.C.L.J. 207 (1979), for an excellent analysis of the EFT legislation.

87. 15 U.S.C. § 1693q (1978).

88. *Id.* § 1693i.

89. *Id.* § 1693c(a)(7).

90. *Id.* § 1693c(a)(1)-(9).

91. *Id.* § 1693c(a)(1)-(5).

92. *Id.*

sent to the consumer,⁹³ generally on a monthly basis. If no transfers have occurred during the month, a statement need be sent only every three months. The periodic statement must provide the same information as supplied on the receipt.⁹⁴

Liability for unauthorized transfers is the key area of the Act. An "unauthorized transfer" is one in which a third person has initiated the transaction without actual authority from the consumer, and the consumer receives no benefit.⁹⁵ If a card is unsolicited, there is no liability to the consumer until the consumer requests validation of the means of access.⁹⁶ Even if the consumer has requested the card, there is no risk to the consumer until receipt.⁹⁷

Thereafter, risk allocation depends upon the involvement of the card in the resulting loss. In the case of a forged card or an intercepted communication, the consumer bears no liability under any circumstances.⁹⁸ If the loss is due to a lost or missing card which is promptly reported, the consumer is liable only for the lesser of \$50 or the amount of the loss, either at the time of notification to the financial institution or when the financial institution otherwise becomes aware that an unauthorized transfer has or may have been effected.⁹⁹ If a missing card is not reported within two days of its loss, or if an error on a periodic statement is not reported within sixty days of receipt of the statement, the consumer may be liable for up to \$500 of losses which would not have resulted but for the failure of the consumer to report the card loss or the error.¹⁰⁰

If the consumer acts in concert with a third person with fraudulent intent to initiate a transfer, or entrusts a third person with the means of access to the account, the consumer is totally liable.¹⁰¹

If the financial institution has failed to make a transfer or a deposit, or has failed to stop payment of a preauthorized transfer as ordered, the financial institution is liable for the damages proximately caused.¹⁰² The financial institution can avoid this liability only by demonstrating by a preponderance of the evidence that its failure to act properly was due to an act of God or other circumstance beyond its control, despite all reasonable precautions to the

93. *Id.* § 1693d(c).

94. *Id.*

95. *Id.* §§ 1693d(11), 1693g(a)(1) & (2).

96. *Id.* § 1693g(a).

97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.*

101. *See id.* § 1693a(11).

102. *Id.* § 1693h(a).

contrary, and that it acted diligently under the circumstances.¹⁰³

The Act also establishes an error resolution procedure.¹⁰⁴ Error is broadly defined and the financial institution is responsible for handling the procedure for resolution of these errors. Such "errors" include allegedly unauthorized transactions, errors of computation, and incorrect transfers of amount or receipts of money.

The consumer may provide written or oral notification of any error within sixty days of receipt of documentation of the transaction, and the financial institution must investigate the possible error, determine whether it is true, and report the result to the consumer within ten business days of the notice.¹⁰⁵ If it is determined that no error occurred, the financial institution must make its findings known within ten business days of the original notice or three days after the determination, whichever is earlier.¹⁰⁶ The financial institution may extend its investigation time to forty-five days by provisionally crediting the consumer's account when the first notice is received.¹⁰⁷

The law allows oral notification of the error by the consumer.¹⁰⁸ However, the financial institution may require written confirmation within ten business days, if the consumer is so informed at the time the oral notice is supplied, and is given an address to which the confirmation should be sent.¹⁰⁹

A right of reversibility, analogous to the stop payment right in the paper-based system but more limited, was debated but not included in the Act.¹¹⁰ There is, however, a stop payment right for preauthorized transfers which may be effected by written or oral notice to the financial institution at any time up to three business days preceding the scheduled date of such transfer.¹¹¹

The Act provides for civil liability against a financial institution which has violated any provision of the Act. This may take the form of actual damages plus, in an individual action, nominal damages of \$100 to \$1,000, attorney's fees and court costs.¹¹² Class action liability may result in actual damages in an amount up to the lesser of \$500,000 or one percent of the defendant's net worth, plus costs and

103. *Id.* § 1693h(b).

104. *Id.* § 1693f.

105. *Id.* § 1693f(a)(3).

106. *Id.* § 1693f(d).

107. *Id.* § 1693f(c).

108. *Id.* § 1693f(a)(3).

109. *Id.*

110. See Greguras & Wright, *supra* note 86, at 250.

111. 15 U.S.C. § 1693h(a)(3) (1978).

112. *Id.* § 1693m(a)(1)-(3).

attorney's fees.¹¹³

In terms of criminal liability, any person who knowingly and willfully fails to comply with the provisions of the law is subject to a fine of not more than \$5,000 and imprisonment of not more than one year.¹¹⁴ A third party who manufactures, uses or distributes counterfeit, fictitious, altered, forged, stolen or fraudulently obtained debit instruments is subject to a fine of up to \$10,000 and imprisonment for up to ten years.¹¹⁵

There are also eleven states which have varying degrees of protection for consumers of EFT services.¹¹⁶ They are Alabama, Colorado, Florida, Iowa, Kansas, Michigan, Minnesota, Montana, New Mexico, Virginia and Wisconsin. Though federal law preempts state laws which provide a lesser degree of protection to consumers,¹¹⁷ it is not clear how this preemption will operate. For example, will a state's entire law be preempted or merely the specific portion which provides less protection than the EFT Act? Until this problem is clarified by regulation, the adoption of consumer protection practices by financial institutions will be slowed and consumer acceptance of EFT services may suffer.

IV. PRIVACY FOR EFT ACCOUNT HOLDERS

The problem of privacy is not unique to the electronic funds transfer area.¹¹⁸ An electronic funds transfer system produces transaction information and data in a different, albeit similar, form to the type of information available in a paper-based check system. As Mr. Justice Douglas observed in *California Bankers Association v. Schultz*:¹¹⁹

In a sense a person is defined by the checks he writes. By examining them the agents get to know his doctors, lawyers, creditors, political allies . . . and so on ad infinitum. These are all tied to one's social security number; and now that we have data banks, these other items will enrich that storehouse and make it possible for a bureaucrat—by pushing one button—to get in an instant the names of the 190 million Americans who are subversives or potential and likely candidates.¹²⁰

113. *Id.* § 1693m(b).

114. *Id.* § 1693n(a).

115. *Id.* § 1693n(b)-(c).

116. See Greguras & Wright, *The Preemption Dilemma Under the New EFT Act*, 12 U.C.C.L.J. 3 (1979), for an analysis of state consumer protection EFT legislation and the interplay of those state laws with the federal EFT Act.

117. 15 U.S.C. § 1693p (1978).

118. See generally BAXTER, *supra* note 41, at 161 *et seq.*

119. 416 U.S. 21 (1974).

120. *Id.* at 85.

The electronic funds transfer area is no less immune to such manipulative use. Government access without the consent of the customer is a matter of major concern. Since *United States v. Miller*,¹²¹ a customer has no rights in his account records, since they are the business records of the bank.¹²² The Tax Reform Act of 1976¹²³ now requires that notices of an Internal Revenue Service summons be given to the depositor and that the depositor then has fourteen days within which to object.¹²⁴ This provision was a partial response to the *Miller* decision. Various states have introduced laws restricting access to bank records except upon court order or judicial subpoena and legislation has also been introduced in Congress to the same effect.¹²⁵

There is no specific privacy protection provision in the EFT Act. The Right to Financial Privacy Act,¹²⁶ also a part of the Financial Institutions Regulatory and Interest Rate Control Act of 1978, sets forth the customer's rights and federal governmental agencies' duties prior to obtaining records of a customer from a financial institution. The Act sets forth five ways in which the federal government can gain access to these records:

(1) voluntary authorization by the customer, after the customer has been notified of his rights;

(2) administrative subpoena with copies served on the customer together with instructions on how the customer may attempt to prevent access;

(3) judicial subpoena, with copies served on the customer together with instructions on how the consumer may attempt to prevent access;

(4) court-issued search warrant with a copy served on the customer; and

(5) if the above procedures are not possible, written request to the financial institution with a copy to the customer who may attempt to prevent access.¹²⁷

The notice to the customer may not be delayed unless a court finds that issuance of the notice would endanger life or limb, or seriously impede or jeopardize the investigation.¹²⁸ The government

121. 425 U.S. 435 (1976).

122. *Id.* at 440.

123. Pub. L. 94-455 (1976).

124. 26 U.S.C. § 7609 (1976 & Supp. II).

125. *See, e.g.*, NEB. REV. STAT. § 8-1401 (1977); H.R. 8133, 95th Cong., 1st Sess. (1977).

126. 12 U.S.C. §§ 3401 *et seq.* (1978).

127. *Id.* §§ 3404-08.

128. *Id.* § 3409.

must certify to the financial institution that the required notice has been given.¹²⁹ Once an agency obtains the customer's records, they cannot be transferred to any other agency without a certification that they are relevant and necessary, and with notice to the customer.¹³⁰

A financial institution must assemble the requested records upon receipt of any of the five specified demands for production.¹³¹ The Act provides that the financial institution is to be reimbursed for its time and expense, whether or not the government ultimately gains access to the records.¹³² The financial institution is absolved from liability if it releases customer records in reliance on the various government certifications required by the Act.¹³³

The EFT deployment and consumer protection statutes of several states include privacy protection provisions which apply specifically to EFT transactions.¹³⁴ Some statutes merely require that a financial institution establish procedures for the protection of account information.¹³⁵ Others strictly limit the circumstances under which any account information may be released,¹³⁶ and some even make system providers as well as financial institutions jointly liable for violation of the privacy protection provisions.¹³⁷

Though there is currently no case law on the privacy rights of account holders, this is almost certain to be an area of future litigation, since there is increasing concern among members of the general public about the potential for intrusion on its privacy made possible by such technological developments as EFT.

V. CONCLUSION

Notwithstanding the problems confronting the development of EFT, the law must surely adjust to accommodate this new technology.¹³⁸ It is only a matter of time until the thicket created by restric-

129. *Id.* § 3403(b).

130. *Id.* § 3412(b).

131. *Id.* § 3411.

132. *Id.* § 3415.

133. *Id.* § 3417(c).

134. See Greguras & Wright, *supra* note 116, for a complete analysis of state provisions.

135. NEB. REV. STAT. §§ 8-1401, -1402 (1979); COLO. REV. STAT. § 11-65-104(1)(a)(iv) (1978).

136. MICH. COMP. LAWS § 488.12 (1978).

137. N.M. STAT. ANNO. § 58-16-12 (1978).

138. Convinced of the need for congressional control over the development of EFT, Congress created the National Commission on Electronic Fund Transfers in 1974. 12 U.S.C. §§ 2401 *et seq.* (1974). The Commission's report was released on March 2, 1977. NAT'L COMM'N ON ELECTRONIC FUND TRANSFERS, EFT AND THE PUBLIC INTEREST (1977).

tive branch banking laws is cleared and the proper sphere of governmental participation and private enterprise is determined. It remains to be seen how the legal and public policy choices will restrict its potential technological development. No "Bell System" for a national EFT service is forming, so the only apparent sponsor on the national level seems to be the Federal Reserve System. The states, however, are expected to fight jealously to retain their own regulatory power. Resolution of this federal-state regulatory dichotomy, or the failure to reach a resolution, may well play a significant part in determining the role that EFT will assume in our monetary system.

Consumer and privacy protection regulations will also affect the eventual role of EFT in our economy. Though it is not clear that enactment of protective laws will immediately increase consumer acceptance and use of EFT services, it is the opinion of financial institution and consumer protection regulators that without legal protection for consumers' transactional rights and informational privacy the eventual level of use will be adversely affected.¹³⁹

At the very least, a definitive resolution of the legal issues which confront those that wish to become involved in EFT is necessary. A business can compute the cost of complying with clearly defined consumer and privacy protection measures, and can analyze deployment legislation and publicly announced antitrust policies in planning an EFT system. A consumer can evaluate the risks involved in the use of these new services if the law is clear and made known. No business and no consumer, however, can analyze or evaluate with any certainty the risks and the costs of EFT until these legal issues are definitively resolved. It may be too much to hope for, but well researched and well written federal legislation could, if it only would, provide a better cure than aspirin for the headaches of persons who must make decisions and plans about EFT today.

The report covers a wide range of areas concerning EFT and is intended to provide Congress with information to aid in structuring a comprehensive and orderly approach to EFT. The Commission submitted its final report in October 1977. NAT'L COMM'N ON ELECTRONIC FUND TRANSFERS, EFT IN THE UNITED STATES: POLICY RECOMMENDATIONS AND THE PUBLIC INTEREST (1977).

139. See Greguras & Wright, *supra* note 86, at 257.