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The Impact of the Federal EFT Act on Customer Contracts in New York State

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Introduction

THE PURPOSE OF this article is to analyze the impact of the Federal Electronic Fund Transfer Act (EFTA)¹ on the unregulated use of electronic fund transfer (EFT) contracts in New York State.² This article discusses a number of common problems facing

1. Title XX of the Financial Institutions Regulatory and Interest Rate Control Act, Pub. L. No. 95-630, § 2001, 92 Stat. 3641 (1978) (to be codified at 15 U.S.C. § 1692).

2. The New York State Consumer Protection Board conducted a survey, during March, April, and May of 1978, to determine what protections, if any, state-chartered banks in New York were extending to EFT customers. NEW YORK STATE CONSUMER PROTECTION BOARD, ELECTRONIC FUND TRANSFERS IN NEW YORK STATE: A STUDY OF THE PRACTICES OF NEW YORK STATE CHARTERED BANKS (1978) [hereinafter cited as EFT SURVEY] (copy of the survey on file in the U.S.F. L. Rev. Office). The survey was conducted by Catherine McCormack, Consumer Affairs Specialist. This survey was completed prior to the enactment of the EFTA. The survey included only the banks that offered automatic teller machines (ATM) or point-of-sale (POS) terminal services. The information derived from this survey will be regularly referred to throughout this article.

The survey covered the eighteen state chartered banks that filed applications as of May 1978, to establish electronic branches with the New York State Superintendent of Banks and actually offer EFT. Ms. McCormack telephoned three branches of each bank and initiated the interview by asking for the officer or person who could give her information about the bank's EFT. She presented herself as a potential customer interested in learning about the bank's electronic banking services. She asked a series of questions about her rights and liabilities, and requested a written disclosure statement. EFT SURVEY, *id.* at 3. Disclosure statements and/or promotional materials were sent by all eighteen banks, although followup telephone calls and formal letters were required to obtain the written materials. Three of the

users of checks, credit cards, and EFT and the treatment of the problems by the laws regulating these payment systems prior to the enactment of the EFTA.³ These laws are compared to the customer's rights and liabilities in EFT contracts of New York State chartered banks. Also, the impact of the EFTA on these customer contracts is analyzed. Finally, ways to comply with the disclosure requirements of the EFTA are suggested, and a sample disclosure statement is offered. It will be concluded that bank contracts must be rewritten in order to comply with the provisions of the EFTA.

I. DISCLOSURE IN READILY UNDERSTANDABLE LANGUAGE IN EFT CUSTOMER CONTRACTS

The ability of consumers to make informed financial decisions depends in large measure on the quality of information provided by financial institutions. The need for financial institutions to provide clear disclosures of rights and liabilities to their customers has been recognized in a series of legislative enactments for checks and credit cards. In 1968, in response to the banking industry's failure to provide meaningful disclosure of credit terms, Congress intervened in the marketplace and mandated full disclosure of credit terms, "so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit."⁴ This landmark statute, popularly known as the Truth-in-Lending Law,⁵ put the banking industry on notice that customers need and should expect "each creditor . . . to disclose clearly and

eighteen banks did not provide an EFT customer contract, leaving fifteen bank contracts for analysis. *Id.* at 7.

For purposes of this article and the survey, New York State definitions of ATM and POS terminals will be used. ATM "mean[s] electronic devices, either on-line or off-line, which permit deposits, withdrawals, transfers of funds from one account to another, loan repayments or disbursements of funds pursuant to pre-arranged lines of credit. Except for the facilities manned for the purposes cited in section 73.10(a) of this Part, they shall not include manned facilities." 3 N.Y.C.R.R. § 73.2 (1977). POS terminals:

Mean electronic devices, either on-line or off-line, whose function is to transfer funds or record transfers of funds in connection with the sale of goods or services but which may also be used to accept deposits and loan repayments, make cash withdrawals and obtain funds pursuant to pre-arranged lines of credit. These terminals may be located only at bona fide checkout counters, cashier stations, customer convenience counters or other counters at which store functions are performed or sales desks of other establishments and may not be manned by bank employees, with the exceptions noted in section 73-10(a) of this Part.

Id.

3. See text accompanying notes 4-10 *infra*.

4. 15 U.S.C. § 1601 (1976).

5. *Id.* §§ 1601-1667e (1978).

conspicuously”⁶ the terms of the bank-customer relationship.

In 1972, Congress required credit card issuers to give “adequate notice to the cardholder of the potential liability”⁷ for the unauthorized use of a credit card. Two years later, Congress prescribed that credit card issuers must transmit a statement to customers describing the new procedures for correcting credit card billing errors,⁸ and the Federal Reserve Board (FRB) promulgated regulations mandating that this notice be “written clearly and conspicuously.”⁹

Still more recently, the New York State Legislature continued this theme of clear disclosure by enacting a plain language law that avoided Congress’ ad hoc approach and required that consumer bank contracts “be written in a clear and coherent manner using words with common and everyday meanings.”¹⁰

In spite of this series of congressional enactments and the unique New York State requirement for clear and coherent disclosure, the New York State chartered banks have failed to provide clear disclosures in their customer EFT contracts.¹¹ A comparison of the EFT contracts offered by fifteen New York State chartered banks and the promotional materials for EFT provided by thirteen of these banks demonstrate the difference between mere disclosure and meaningful disclosure.¹² It is apparent that some banks took greater care to insure that their contracts were able to be easily read

6. *Id.* § 1631 (1974); 12 C.F.R. § 226.6 (1978).

7. 15 U.S.C. § 1643 (1978).

8. *Id.* § 1637(a)(8).

9. 12 C.F.R. § 226.7(d)(1) (1978).

10. N.Y. GEN. OBLIG. LAW § 5-702 (McKinney Supp. 1978). The requirement applies to “every written agreement . . . to which a consumer is a party and the money, property or service which is the subject of the transaction is primarily for personal, family, or household purposes” *Id.* This statute was signed into law on August 5, 1977, but did not become effective until November 1, 1978, after completion of our survey of customer contracts. See also The Magnuson-Moss Warranty Act, 15 U.S.C. § 2303 (Supp. 1978); 16 C.F.R. § 701.3 (1978) (requires simple and readily understood disclosure of warranty terms). By May 1978, at least ten states, including New York State, enacted statutes or promulgated regulations requiring disclosure of rights and liabilities to EFT customers. ALA. STATE BANKING DEPT., EFT Sys. REGS. (1976); FLA. STAT. ANN. § 659.062 (West Supp. 1978); IOWA CODE ANN. § 527.1-.12 (West Supp. 1978); MONT. REV. CODES ANN. §§ 5-1701 to 1721 (Supp. 1977); New York Banking Regs. § 73.5(k) (1978); N.D. DEPT. BANKING & FIN’L INST., REG. FOR ESTAB. OF CUSTOMER EFT CENTERS, ch. 13-02-06 (1976); OR. COMMERCE DEPT., BANKING DIV. ADMIN. RULES, §§ 805-16-210 to 230 (1976); R.I. DEPT. BUS. REG., BANKING DIV., CBCT APPLICATION REQUIREMENTS (1975); VA. STATE CORP. COMM’N, EFT REGS. (1977); Wis. Admin. Code, ch. S & L26 (1976).

11. EFT SURVEY, *supra* note 2, at 4-5. Furthermore, thirteen of the fifteen banks provided the New York State Consumer Protection Board researcher with incomplete or inaccurate information over the telephone when compared with the EFT customer agreement. *Id.* at 9.

12. Some of the promotional materials and EFT contracts are on file in the U.S.F. L. Rev. Office.

and understood.¹³ The more conscientious banks simplified the contractual language, removed unnecessary provisions, and designed the forms to include contrasting large and small print, descriptive headings and subsections, two-column format, and colored type and paper.¹⁴ However, even when customer contracts of the more conscientious banks are compared to promotional material used by all the banks to entice new EFT customers, the shortcomings of all the contracts are clear and the potential for readable contracts becomes obvious. The banks artfully designed the promotional materials distributed to potential customers to convey a clear and practical description of the electronic banking services.¹⁵ When compared to the contracts, the promotional materials were printed in more simplified language and with more effective use of large and bold print.¹⁶

One bank made it easy to compare the readability of its contract to its promotional material by printing both items on one long page.¹⁷ The top half of the page is a request form for the EFT card where the bank condensed in the middle of the form the terms of the contract in small print and without spaces between paragraphs, without contrasting print, and without any descriptive headings.¹⁸ The contract is not even labeled a contract, agreement, or with any similar description. Buried in the fine print in the second column and the second paragraph of this contract, the customer agrees to be liable for all transactions initiated with the EFT card and the personal identification number (PIN) with respect to the customer's checking account, and agrees to be liable for only authorized transactions with respect to his or her savings account.¹⁹

In contrast, the lower half of the page describes the EFT service by using larger print than for the contract, bold and contrasting print, descriptive headings in a different color than the other print, and well spaced sections.²⁰ The bank employed pictures, numbered sections in a third color, and clearly separated steps to explain how to use the card.²¹ There is no reason why the bank could not have

13. For a detailed text on drafting readable contracts, see C. FELSENFELD & A. SIEGEL, *SIMPLIFIED CONSUMER CREDIT FORMS* (1978); R. FLESCH, *HOW TO WRITE, SPEAK, AND THINK MORE EFFECTIVELY* (1960).

14. See Promotional Material and Contracts, *supra* note 12.

15. *Id.*

16. *Id.*

17. *Id.* See Promotional Material, Marine Midland Bank, Melville, New York (on file at U.S.F. L. Rev. Office).

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id.*

used the same communication techniques it used to explain the EFT services to its customers to also convey to its customers their rights and liabilities.

Furthermore, none of the promotional materials we reviewed described all the terms and conditions written into the customer contracts.²² The most important omission from the promotional materials was the provision on the customer's liability for the unauthorized use of the debit card.²³

Based on this study of the EFT contracts offered by the New York State Chartered Banks, Congress acted appropriately in mandating that financial institutions disclose "the terms and conditions of electronic fund transfers involving a consumer's account . . . in readily understandable language."²⁴ As banks throughout the nation start to draft contracts to comply with the EFTA, they should avoid the discrepancy that exists in New York State between the contracts and promotional materials and draft the contracts to provide "clear and informative"²⁵ disclosures to their customers.

II. DISCLOSURE OF TERMS AND CONDITIONS IN EFT CUSTOMER CONTRACTS

The EFTA not only requires disclosure in readily understandable language, but it also creates and describes the terms and conditions to be disclosed to customers.²⁶ It establishes the maximum customer liability for unauthorized electronic fund transfers,²⁷ the procedures for error resolution,²⁸ the consumer's right to receive documentation,²⁹ and the financial institution's liability.³⁰ Section 905 discusses the terms and conditions that must be disclosed³¹ and the conspicuous omission of mandatory disclosure of any right to reverse transactions.

The most important consumer protection in the EFTA is the

22. See EFT SURVEY, *supra* note 2, at 5.

23. *Id.* at 4.

24. EFTA § 905, *supra* note 1.

25. S. REP. No. 915, 95th Cong., 2d Sess. 12 (1978).

26. EFTA § 905, *supra* note 1.

27. *Id.* § 909.

28. *Id.* § 908.

29. *Id.* § 906.

30. *Id.* § 910.

31. The EFTA also requires disclosure of the bank's telephone number and address, the type and nature of electronic fund transfers that the consumer may initiate, any charges for EFT or the right to make such transfers, and under what circumstances the bank will disclose information concerning the consumer's account to third persons. *Id.* § 905.

customer liability section for unauthorized use because it establishes the rules for allocating the risks of unauthorized use between the bank and the customer.³² The possible extent of loss for the customer in an EFT environment is immense. All an unauthorized user needs is knowledge of the PIN and possession of the debit card to have access to the customer's entire bank account.

A customer liability section must provide the customer sufficient financial incentive to protect the security of his or her debit card and PIN. Simultaneously, the provision must also provide the bank sufficient financial incentive to design a secure EFT system. The same type of accommodating of incentives had to be done for the check and credit card systems.

The Uniform Commercial Code provides the banks an incentive to design a system that guards against the unauthorized use of checks by creating three conditions precedent before the bank can impose any liability on its customers. The bank must prove that a customer was negligent, that this negligence substantially contributed to the material alteration of an instrument or to the making of an unauthorized signature, and that the bank acted in a commercially reasonable manner in paying the check.³³

In contrast, Congress rejected a negligence standard for credit cards. It established instead a new and different type of liability provision for credit card users to encourage responsible use and the development of a safe credit card system.³⁴ A credit cardholder's liability is limited to fifty dollars, even if the loss results from the cardholder's negligence.³⁵

32. *Id.* § 909.

33. U.C.C. § 3-406 (1972 version). As of May 1978, three states had adopted a somewhat similar negligence standard for debit cards. FLA. STAT. ANN. § 659-062(13)(a) (West Supp. 1978); MONT. REV. CODES ANN. § 5-1713 (Supp. 1973); VA. CODE § 6.1-39.1 (Supp. 1978).

34. Weistart, *Federal Control of Credit Cards*, 70 MICH. L. REV. 1475, 1508 (1972).

35. 15 U.S.C. § 1643 (1974). Section 1643 limits a credit cardholder's liability for unauthorized use of the card to the lesser of fifty dollars or to when the bank learns of the loss of the card. The card issuer must also provide adequate notice of this liability and furnish to the cardholder a self-addressed, prestamped notification to be used in the event of a lost or stolen card. If any of these conditions are not met, or if the issuer has not provided a method whereby the user of a credit card can be identified as the person authorized to use it, the cardholder has no obligation for the unauthorized use of the credit card. *Id.* As of May 1978, at least five states similarly limited customer liability for unauthorized use of a debit card. COLO. REV. STAT. § 11-6.5-109(2) (1978); IOWA CODE ANN. § 527.8 (West Supp. 1978); KAN. STAT. § 17-5569 (1975); N.M. STAT. ANN. § 48-25-13(B) (1977); Wis. Admin. Code, S & L § 26.07(2)(a) (1976). Two other states enacted similar laws effective after completion of our survey in May 1978. 1978 Mich. Pub. Acts No. 322, § 14; 1978 Minn. Laws, ch. 469, § 9(3). Another state imposes on the customer unlimited liability until the bank receives notice of the lost or stolen card. ALA. STATE BANKING DEP'T., EFT SYS. REGS. (1976).

Whether a limited liability provision in the amount of fifty dollars exposes an EFT customer to more or less liability than a negligence standard depends on the specific facts of the case.³⁶ Nevertheless, the majority position in the Senate report that recommended the adoption of the fifty dollar ceiling approach in the EFTA concluded that:

In deliberating this issue, the committee considered, but rejected, a standard which would determine the consumer's liability on whether the consumer acted in a specified negligent manner. While this approach has the attribute of specifically requiring careful conduct by the consumer, the committee believes it presents considerable problems, such as the vagueness of the standards, how to prove that the consumer (and not a thief) engaged in the proscribed conduct, and the potential for widespread litigation over these points which would leave the consumer without his funds while these questions are before the courts. For these reasons, the negligence approach was rejected.³⁷

Congress apparently agreed with the committee that the dollar ceiling approach provides greater protection for consumers of EFT than a negligence standard, since the EFTA provides a dollar limitation on liability.³⁸

The contracts of fourteen of the fifteen New York State chartered banks analyzed in the study imposed on their customers greater liability than they imposed on users of checks and credit cards.³⁹ The fourteen banks set no dollar limit on their EFT customer's potential liability.⁴⁰

The EFTA will require all banks to revise their contracts to reduce their customer's share of the liability for unauthorized use

36. Situations could be hypothesized where a customer's liability will be greater with a limited liability provision of fifty dollars than with the application of a negligence standard.

37. S. REP. NO. 915, 95th Cong., 2d Sess. 6 (1978).

38. EFTA § 909, *supra* note 1.

39. EFT SURVEY, *supra* note 2, at 4.

40. *Id.* Of the fourteen banks, two banks imposed complete liability on their EFT customers for all transactions whether authorized by the customer or not. Three banks imposed complete liability for all transactions until the bank receives notice that a card had been lost or stolen. One bank imposed complete liability for all transactions that occurred before the bank received notice that a card is missing, plus an additional liability of up to fifty dollars even after the bank receives notice. Eight banks did not explicitly mention liability. Instead, they required their customers to agree to care for their debit cards and PIN in a prudent manner, and/or to take all steps necessary to protect the security of their cards and PIN. These agreements did not inform customers whether they were liable for unauthorized transactions if the bank determined that they had not acted in a prudent manner. One bank did not impose any liability on its customers for the unauthorized use of a debit card. *Id.* at 7-8.

of the debit card.⁴¹ The banks do not have to adopt the exact terms of the EFTA, only limit the liability of their customers to an amount no greater than permitted by the EFTA.⁴²

The customer liability provision of the EFTA establishes a three-tier structure for determining the customer's liability for the unauthorized use of a debit card.⁴³ The liability section in the EFTA is a complex modification of the law that applies to credit cards that expose the EFT customer to greater liability than that of a credit card customer.⁴⁴ It is also a modification of the checking customer's duty to examine checks and banking statements.⁴⁵

The first and second tier of liability limits the customer's maximum losses to either fifty or five hundred dollars depending on when the customer notifies the financial institution of a lost or stolen debit card. If the customer notifies the financial institution that the debit card is lost or stolen within two business days after learning of it, or within a reasonable time under extenuating circumstances, the customer will only be liable for the lesser of fifty dollars or actual losses incurred prior to the bank receiving notice that the card was lost, stolen, or used without the customer's authorization.⁴⁶

If the customer fails to notify the financial institution about any loss or theft of the debit card within two business days, the customer may be liable for any losses that occur after those two business days, or in extenuating circumstances, a reasonable time thereafter.⁴⁷ The extent of liability is the lesser of five hundred dollars or actual losses incurred prior to the financial institution receiving notice that the card was lost, stolen, or used without the customer's authorization.⁴⁸ In addition, the financial institution must

41. EFTA § 909, *supra* note 1.

42. *Id.* § 909(d).

43. *Id.* § 909.

44. *Compare id.* § 909 with 15 U.S.C. § 1643 (1978).

45. *Compare* EFTA § 908, *supra* note 1, with U.S.C. § 4-406 and 15 U.S.C. § 1666(a) (Supp. 1978).

46. EFTA § 909(a)(2), *supra* note 1. Adequate notice includes the financial institution becoming:

[A]ware of circumstances which lead to the reasonable belief that an unauthorized electronic fund transfer involving the customer's account has been or may be effected. Notice . . . is sufficient when such steps have been taken as may be reasonably required in the ordinary course of business to provide the financial institution with the pertinent information, whether or not any particular officer, employee, or agent of the financial institution does in fact receive such information.

Id.

47. *Id.* § 909. The EFTA notes such extenuating circumstances as extended travel or hospitalization. *Id.* § 909(a)(2).

48. *Id.* § 909.

show that it could have prevented the losses had it been notified within the two business days or the reasonable time.⁴⁹

The third tier exposes the customer to complete liability if he or she fails to notify the financial institution of any unauthorized transactions or errors within sixty days of the transmittal of the periodic statement or within a reasonable time under extenuating circumstances.⁵⁰ The financial institution does not have to reimburse the customer for any losses occurring after the sixty days or the reasonable time period. However, the financial institution must show the loss would not have occurred but for the failure of the customer to report within the sixty days or a reasonable time.⁵¹

The question remains whether the three-tier liability section will prove to be too complicated and confusing for customers to encourage careful use of debit cards. Any confusion may be compounded by the physical similarities between credit cards and debit cards.⁵²

The other side of this question is whether subjecting the bank to less liability than with credit cards will significantly diminish the financial institution's incentive to implement improved security procedures such as voice or fingerprint recognition or signature verification. This unique three-tier liability system for EFT customers needs to be monitored to determine whether an effective balancing of incentives occurs.

III. ERROR RESOLUTION

The complexity of EFT, the reduced amount of physical records, and the financial institution's complete control over the design and operation of the EFT system make the customer's proof of an error extremely difficult. Because an electronic fund transfer provides access to the entire account of a consumer, an error could leave the consumer with little or no cash assets, pending resolution of the error. The expense of litigating the existence of an error could cost more than the amount involved in the dispute. Consequently, a fair, expeditious, and nonjudicial error correction procedure is needed for electronic fund transfers.

Responding to a similar need for the resolution of credit card billing errors, Congress recently enacted the Fair Credit Billing Act

49. *Id.*

50. *Id.*

51. *Id.* Cf. U.C.C. § 4-406 with EFTA § 909, *supra* note 1.

52. EFT SURVEY, *supra* note 2, at 4.

(FCBA).⁵³ This Act requires a card user to notify the card issuer in writing within sixty days of receiving his or her periodic statement, if the consumer believes that an error has occurred.⁵⁴ The issuer has ninety days to complete its investigation and either correct the error or provide the consumer with a written explanation of why the issuer believes that no error occurred.⁵⁵

Despite this precedent, none of the New York bank agreements analyzed in the state provided their customers with any error resolution procedures.⁵⁶ The EFTA changes this by mandating formal procedures that consumers and financial institutions must follow if a consumer alleges that an error exists. As with the FCBA, the EFTA imposes an initial duty on the consumer to examine his or her transaction receipts and periodic statements and to notify the financial institution of any errors within sixty days.⁵⁷ Once the financial institution receives notification that the consumer believes an error has occurred, the EFTA grants the financial institution up to ten days to investigate the error and to report or mail the results of its investigation to the consumer.⁵⁸ The time period can be extended to forty-five days if the bank provisionally recredits the consumer's account within ten business days pending the completion

53. 15 U.S.C. §§ 1666-1677 (Supp. 1978). While the U.C.C. does not contain a formal error resolution procedure, a financial institution that improperly pays out on an item must recredit its customer's account and seek redress against any culpable third party. U.C.C. § 4-401 (1972 version). See J. WHITE & R. SUMMERS, *UNIFORM COMMERCIAL CODE* § 17-3 (1972).

54. 15 U.S.C. § 1666(a) (Supp. 1978).

55. *Id.* § 1666(a)(3)(B). By May 1978, four states had enacted similar procedures for resolving EFT errors. However, in contrast to the FCBA, the financial institutions have between ten and ninety days, depending on the state, to act on the consumer's complaint. IOWA CODE ANN. § 527.8 (West Supp. 1978) (ninety days); MASS. ANN. LAWS. Ch. 167, § 65 & Ch. 93C, § 3 (Michie/Law. Co-op 1977 & 1978) (sixty days or ninety days where information from a third party seller of goods is needed to correct the error); 1978 Mich. Pub. Acts No. 322, § 15(1) (ten days); MONT. REV. CODES ANN. § 5-1712 (Supp. 1977) (ten days).

56. EFT SURVEY, *supra* note 2, at 4. All of the New York State chartered banks surveyed contend that they informally resolve every purported error. *Id.* at 12. The informal procedures, however, depend on the good faith of the financial institution, an inadequate substitute for contractual or statutory rights.

57. EFTA § 908, *supra* note 1. In contrast to the FCBA, the notice may be either written or oral. Compare *id.* § 908(a) with 15 U.S.C. § 1666(a) (Supp. 1978). The notice must also be sufficient to enable the financial institution to identify the name and account number of the consumer, the amount of the error, and the reasons for the consumer's belief that an error has occurred. EFTA § 908(a), *supra* note 1. The FCBA imposes similar requirements. 15 U.S.C. § 1666(a) (Supp. 1978).

58. EFTA § 908(a), *supra* note 1. If the initial notification is oral, the financial institution may require the consumer to provide the financial institution with written confirmation within ten days. The financial institution, however, must still investigate and report its findings to the consumer within ten days of the original oral notice. *Id.*

of its investigation.⁵⁹ The time period for investigation of EFT errors is substantially shorter than for credit card errors because an EFT error may result in an immediate loss of funds while a credit card error simply results in an erroneous bill.⁶⁰ The financial institution also must notify the consumer that he or she has a right to request copies of all the documents that the institution relied on in making its findings of no error.⁶¹ The FCBA does not have a similar requirement for credit card disputes.⁶²

Ten days for the bank to act on a consumer's EFT complaint is a clear improvement over the lack of any formal error resolution procedures in the customer contracts. However, over half the banks surveyed indicated that in most instances they could trace and resolve an error within three business days.⁶³ Moreover, it has been suggested that ten days is too long for consumers to have their funds tied up and shorter time periods have been recommended.⁶⁴

IV. DOCUMENTATION

An EFT system replaces the customer's signed receipts that are used as records of transfers with electronic impulses. The elimination of the paper documents without an adequate substitute limits the ability of consumers to manage their financial affairs.

The consumer's need for documentation of his or her financial activities is provided for in both the checking and credit card payment systems. A check provides the consumer with a reliable signed written record of a transaction. The amount, date, and payee are all printed on the check, which ordinarily is returned to the consumer along with a monthly statement. Credit card users are also given a signed, written receipt indicating the amount, date, and the seller's name, which is provided to the consumer at the time of sale. In addition, a credit card issuer must transmit to the consumer periodic statements that at a minimum identify the goods or services

59. *Id.*

60. S. REP. NO. 915, 95th Cong., 2d Sess. 7 (1978).

61. EFTA § 908(d), *supra* note 1.

62. See 15 U.S.C. § 1666(a)(3)(B)(ii) (Supp. 1978); 12 C.F.R. 226.14(a)(2)(iii) (1970).

63. EFT SURVEY, *supra* note 2, at app. C.

64. *Proposed Amendments to the Consumer Credit Protection Act: Hearings on H.R. 8753 Before the Subcomm. on Consumer Affairs of the House on Banking, Finance and Urban Affairs, 95th Cong., 1st & 2d Sess. 106 (1977-1978)* (statement of Jim Brown, Center for Consumer Affairs, University of Wisconsin Extension); *id.* at 532 (statement of Ellen Broadman, Consumer Union); *id.* at 182 (statement of the Hon. Ester Peterson, Special Assistant to the President for Consumer Affairs) [hereinafter cited as *House Hearings*].

purchased, the date of the transaction, and the amount.⁶⁵

Although none of the New York State chartered bank agreements examined provide for documentation,⁶⁶ all the banks did offer their customers transaction receipts and periodic statements.⁶⁷ The EFTA, therefore, will not significantly alter existing practices, except to the extent that it mandates specific information on transaction receipts and periodic statements,⁶⁸ insures the continuation of documentation for consumers,⁶⁹ and permits the documentation to be admissible as evidence and *prima facie* proof of a transfer.⁷⁰

V. LIABILITY OF FINANCIAL INSTITUTIONS

The failure of a financial institution to transfer money as instructed by the customer can expose the customer to damages that may exceed the amount of money involved in the transaction. For instance, if the bank erroneously refuses to pay a customer's premium for fire insurance and the customer's house is damaged by fire, the amount of damages will probably far exceed the insurance premium. If the consumer paid the insurance premium with a check, the Uniform Commercial Code holds the bank liable for "damages proximately caused by the wrongful dishonor"⁷¹ of the check. "When the dishonor occurs through mistake, liability is limited to actual damages proved."⁷²

65. 15 U.S.C. § 1637(b) (Supp. 1978); 12 C.F.R. 226.7(k) (1978). As of May 1978, at least seven states recognized the need for documentation for EFT and mandated transaction receipts and/or periodic statements for users of EFT. Similar to the requirement for credit cards, these states commonly provide for a periodic statement containing a description of all transactions sufficient to enable the account holder to identify all transfers and to relate them to his or her transaction receipts. IOWA CODE ANN. § 527.6 (West Supp. 1978); 1978 Mich. Pub. Acts No. 322, §§ 17, 18; 1978 Minn. Laws, ch. 469, § 9(6); MONT. REV. CODES ANN. § 5-1711 (Supp. 1977); N.M. STAT. ANN. § 48-25-12(D) (1977); VA. STATE CORP. COMM'N, EFT REGS. § 12 (1977); Wis. Admin. Code, ch. S & L 26, § 8 (1976).

66. EFT SURVEY, *supra* note 2, at app. C.

67. *Id.*

68. EFTA § 906, *supra* note 1. The EFTA requires transaction receipts to be made available at the time of the transfer. The receipt must include the type, amount, and date of transfer and identify the consumer's account, the location of the electronic terminal involved in the transaction, and the third party to whom or from whom funds are transferred. Consumers must also be provided with periodic statements, which include all the information required on a receipt as well as the opening and closing account balance, any fees charged, and an address and telephone number where errors may be reported. The statement may also include financial information about other non-EFT accounts. *Id.*

69. *Id.*

70. *Id.*

71. U.C.C. § 4-402 (1972 version).

72. *Id.*

If the consumer paid the insurance premium through an EFT system prior to the effective date of the EFTA, and the bank failed to transfer the money, it is unclear how the liability would be allocated between the bank and the customer. In New York State, the study indicates that only two of the fifteen contracts for the state chartered banks mention bank liability, and both banks limit the bank's liability to the amount improperly debited and specifically disclaim any liability for consequential damages.⁷³

The EFTA prevents the banks from trying to limit their liability so narrowly.⁷⁴ The EFTA also clarifies the liability for the rest of the banks by establishing a bank liability section substantially similar to the rules that apply to the checking system.⁷⁵ The EFTA states that the financial institution is liable for all damages "proximately caused" by the "financial institution's failure to make an electronic fund transfer, in accordance with the terms and conditions of an account . . . when properly instructed to do so by the consumer."⁷⁶ The financial institution is also liable for all damages "proximately caused" by its failure to make an "electronic fund transfer due to insufficient funds when the financial institution failed to credit . . . a deposit of funds . . . which would have provided sufficient funds to make the transfer."⁷⁷ However, the EFTA defines a dishonor by mistake in an EFT environment as a failure that was not intentional and resulted from a bona fide error, "notwithstanding the maintenance of procedures reasonably adapted to avoid any such error."⁷⁸ As with checks, the financial institution is then only liable for actual damages.⁷⁹

The major exception to the financial institution's liability is similar for both EFT and the checking system. The financial institution is not liable if its action or failure to act resulted from circum-

73. EFT SURVEY, *supra* note 2, at 7-8 & app. C.

74. EFTA § 910, *supra* note 1.

75. See Broadman, *Electronic Fund Transfer Act: Is the Consumer Protected?* 13 U.S.F. L. REV. 245 (1979).

76. EFTA § 910(a)(1), *supra* note 1. But see *id.* § 910(a)(1)(A)-(E) which sets forth exceptions to the bank's liability: (A) The consumer account has insufficient funds; (B) the funds are subject to legal process or other encumbrance restricting such transfer; (C) such transfer would exceed an established credit limit; (D) an electronic terminal has insufficient cash to complete the transaction; (E) as otherwise provided in regulations of the Board. *Id.*

77. *Id.* § 910(a)(2).

78. *Id.* § 910(c).

79. *Id.* Judicial interpretations of the Uniform Commercial Code's distinction between "actual damages" and "proximately caused damages" should also apply to the application of the EFTA. See White & Summers, *supra* note 53, at § 17-4; U.C.C. Rep. § 4-402 (Supp. 1978).

stances beyond its control and the financial institution "exercised such diligence as the circumstances required."⁸⁰ The provider of EFT must also exercise "reasonable care to prevent such an occurrence" to avoid liability.⁸¹ Therefore, financial institutions will have a special duty to design EFT systems that anticipate such problems as blackouts, brownouts, and earthquakes.⁸²

While it may sound reasonable to protect banks from liabilities that occur for reasons beyond their control, the real impact of the exception is to shift the liability from the financial institution to its customers. Customer contracts should conspicuously disclose this special risk imposed on consumers.⁸³

VI. REVERSIBILITY

Perhaps the most controversial issue surrounding the EFT legislative debates is whether or not the consumer should be allowed to instruct his or her financial institution to reverse a transaction. Consumer spokespeople argue that this right is essential to consumer acceptability of EFT and to insure that protections provided consumers over recent years are not circumvented.⁸⁴ Some financial institutions and merchants contend that reversibility will destroy the marketability of EFT and add to its cost by decreasing the system's efficiency.⁸⁵

Both the check and credit card payment systems provide the consumer with some form of reversibility. The Uniform Commercial Code requires a financial institution to stop payment on any unpaid check if so ordered by a customer, regardless of the reason, provided

80. EFTA § 910(b), *supra* note 1; U.C.C. § 4-108 (1972 version). *See also* EFTA § 910(b)(2), *supra* note 1, which provides another exception to a bank's liability where "a technical malfunction which was known to the consumer at the time he attempted to initiate an electronic fund transfer." *Id.*

81. EFTA § 910, *supra* note 1. A recent decision by the Kentucky Court of Appeals recognized a similar obligation for banks in the checking system. The court would not excuse a bank for circumstances beyond its control when the bank did not plan for the foreseeable increased volume of items to be processed after Christmas. *Blake v. Woodford Bank & Trust Co.*, 555 S.W.2d 589 (1977).

82. *See also* Greguras, *Electronic Fund Transfers and the Financial-Institution/Consumer Relationship*, 10 UNIFORM COM. CODE L.J. 172, 195-98 (1978).

83. *See* Brandel, *Electronic Funds Transfer: Commercial and Consumer Aspects*, 82 COM. L.J. 78, 82 n.29 (1977).

84. *House Hearings*, *supra* note 64, at 537 (statement of Ellen Broadman); *id.* at 64 (statement of Patrick Portway, Virginia Citizens Consumer Council).

85. *Id.* at 407 (statement of Evan H. Housworth, American Bankers Association); *id.* at 1008 (statement of Robert J. Devine, American Retail Federation). *Contra, id.* at 1403 (statement of J. Federic Ruf, President, Tyme Corp.)

notice is given at such a time and in such a manner as to afford the bank a reasonable opportunity to act.⁸⁶ The Federal Consumer Credit Protection Act subjects the issuer of a credit card to all the claims and defenses that could be asserted against the merchant, in effect forcing the issuer to reverse the purchase transaction against the merchant.⁸⁷

In contrast, the EFT study indicates that none of the eight New York State chartered bank agreements that offer or anticipate offering POS terminal services provided their customers with a reversibility right.⁸⁸ Further, three of the banks specifically prohibited the exercise of a reversibility right, even though the consumers have been conditioned by their check and credit card experience to expect this right.⁸⁹ Unfortunately, the EFTA does nothing to remedy this situation. Although consumer witnesses at the congressional hearings testified in support of a reversibility provision⁹⁰ and earlier versions of the bills would have enabled consumers to reverse an electronic fund transfer,⁹¹ this provision was not included in the EFTA.

The omission of a reversibility right in the EFTA leaves a serious gap in the statutory protections the law affords consumers, par-

86. U.C.C. § 4-403 (1972 version).

87. See 15 U.S.C. § 1666(i) (Supp. 1978) (credit card companies are subject to claims and defenses arising out of any transaction in which credit cards are used if: (1) The consumer has made a good faith attempt to obtain satisfaction from the seller; (2) the amount of the initial transaction is more than fifty dollars; and, (3) the place of the initial transaction was in the same state as the cardholder's address or within one hundred miles of that address). Similarly, several states by May 1978, had also established a reversibility right in their EFT statutes or regulations. MICH. STAT. ANN. § 23,1137(16) (1978); N.M. STAT. ANN. § 48-25-14 (1977); Wis. Admin. Code, ch. S-L 26.09 (1976). Typically, these provisions require the financial institution to reverse a transaction against the merchant if the consumer requests reversal within the first few days after the sale and the purchase price exceeds fifty dollars. New Mexico has a limited reversibility right which allows:

A customer of a financial institution may by order to his financial institution stop payment of any negotiable instrument or share draft payable for his account when given to a seller of goods or services who received a verification, limited guarantee or guarantee when used for the purchase of goods or services through use of a point-of-sale terminal.

N.M. STAT. ANN. § 48-25-14 (1977).

88. EFT SURVEY, *supra* note 2, at app. C.

89. *Id.*

90. *House Hearings*, *supra* note 64, at 102 (statement of Jim Brown); *id.* at 86 (statement of Linda Joy, Michigan Consumers Council); *id.* at 180 (statement of the Hon. Ester Peterson); *id.* at 810 (statement of Richard Spohn, California State Department of Consumer Affairs).

91. See H.R. 8753, 95th Cong., 1st Sess. § 806(A)(2) (1977); S. 2065, 95th Cong., 1st Sess. § 808 (1977); S. 2546, 95th Cong., 2d Sess. § 908 (1978).

ticularly since analogous rights are available in alternative payment systems. Reversibility indicates to the consumer that a merchant is willing to stand behind his or her product, at least partially correct the often unequal bargaining position of merchant and consumer, and deter overreaching business practices. Without this right, if the goods delivered are defective or different from the goods the consumer purchased, he or she will have to sue if the merchant refuses to settle the dispute.⁹² Although the vast majority of merchants will satisfactorily resolve consumer disputes, to a certain extent resolution occurs because reversibility is available to the buyer.⁹³

Conclusion

The New York State Chartered Banks need to revise major portions of their customer contracts to conform with the requirements of the EFTA. The banks ignored most of the analogous minimum protections applicable to check and credit card users when drafting their customer contracts. Many of the contracts will have to be rewritten in readily understandable language.⁹⁴ The banks will also need to substantially redraft their contracts to reduce customer liability for unauthorized electronic fund transfers and to provide for formal procedures for error resolution, a right to receive documentation, and the bank's liability for the failure to pay as instructed.

92. See generally H.R. REP. NO. 1315, 95th Cong., 2d Sess. 5 (1978).

93. *House Hearings*, *supra* note 64, at 115 (statement of Jim Brown).

94. A disclosure statement for POS and ATM terminals is provided for reference and discussion. See Appendix A *infra*. Laurie Kramer, Director of Consumer Education for the New York State Consumer Protection Board, edited and simplified the language in the disclosure statement.

The most difficult problem when drafting a disclosure statement is balancing the need for full disclosure against the confusion caused by too much detail and a lengthy disclosure statement. Hearings by the FRB pursuant to § 905(a) of the EFTA should assist financial institutions and consumers in arriving at a balanced disclosure statement. EFTA § 905(a), *supra* note 1. Also, the advice of marketing experts who are skilled in promoting EFT should be helpful in drafting a disclosure statement that effectively communicates rights and liabilities.

See also the sample disclosure form in compliance with S. 3156. S. REP. NO. 915, 95th Cong., 2d Sess. 11 (1978).

APPENDIX A

DISCLOSURE STATEMENT

IMPORTANT INFORMATION ABOUT YOUR CARD
THIS IS A BRIEF DESCRIPTION OF YOUR LEGAL RIGHTS
FOR DETAILS CONTACT AN ATTORNEY

1. HOW TO CONTACT THE BANK

Telephone No.:
Address:

2. WHEN YOU MAY USE YOUR CARD

You may use your card to deposit or withdraw money from your account. You may also use your card to pay for merchandise at participating stores.

3. LIMITS ON USE OF CARD

(describe any limitations on frequency or dollar amount of transfers)

4. WHAT HAPPENS IF YOUR CARD IS LOST, STOLEN, OR USED WITHOUT YOUR PERMISSION

Notify the bank immediately if your card is lost, stolen, or used without your permission. The time periods below will be extended only in limited circumstances such as hospitalization or extended travel.

When Your Losses Are Limited to \$50

If you notify the bank that your card has been lost, stolen, or used without permission within 2 business days after you find out, the bank must reimburse you for any loss that is greater than \$50.

When Your Losses Are Limited to \$500

If you do not notify the bank that your card has been lost, stolen, or used without permission within 2 business days after you find out, you may lose up to \$500 - - but only if the bank proves that it could have prevented these losses had it been notified.

When There Is No Limit On Your Losses

If a periodic statement shows a transfer that you did not make, you have 60 days to notify the bank. If you don't, the bank may not have to reimburse you for any money lost, if the bank proves that it could have prevented these losses had it been notified.

5. WRITTEN RECORDS

The bank will offer you a receipt every time you use your card. In addition, the bank will send you periodic statements describing all the times you used your card during that period. You can use your receipts and statements just like cancelled checks - - as proof that you paid your bills.

6. WHAT TO DO IF THERE ARE ERRORS ON YOUR STATEMENT OR RECEIPTS

If you think there is an error on one of your receipts or periodic statements, you have 60 days to notify the bank in person, by telephone, or in writing. You must tell the bank why you think there's an error. If you tell the bank in person or by telephone, the bank may require you to notify it in writing within 10 days too.

The bank must investigate your complaint and tell you what it finds within 10 days after you notified it. If the investigation takes longer, the bank will put back into your account within those 10 business days the amount you believe to be in error, and will correct any error within 45 days after you first contacted the bank.

If the bank concludes that no error occurred, you will receive an explanation, and if you ask, the bank will also send you copies of all records it relied on.

7. WHAT HAPPENS IF THE BANK DOES NOT FOLLOW YOUR INSTRUCTIONS

When the Bank Is Responsible

If you lose money because the bank did not follow your instructions, the bank usually has to reimburse you for your losses.

When the Bank Is Not Responsible

If you lose money because the bank did not follow your instructions, the bank does not have to reimburse you if your account did not have enough money, if the bank's electronic branch did not have enough cash, or if it can show that you knew the equipment was not working right. The bank also does not have to reimburse you for your losses if the bank can show that it did not follow your instructions because of circumstances beyond its control and that it tried to prevent your losses.

8. CHARGES FOR USE OF THE CARD

(List Charges)

9. PRIVACY

(describe under what circumstances the financial institution, will in the ordinary course of business, disclose information concerning the customer's account to third parties)

EDITOR'S NOTE: This disclosure statement only applies to POS and ATM terminals and does not cover preauthorized transfers.

