

DEPARTMENT OF THE TREASURY

Fiscal Service

31 CFR Part 203

RIN-1510-AA37

Payment of Federal Taxes and the Treasury Tax and Loan Program

AGENCY: Financial Management Service, Fiscal Service, Treasury.

ACTION: Final rule.

SUMMARY: The Financial Management Service is issuing this final rule to implement provisions of the North American Free Trade Agreement Implementation Act (NAFTA), as amended. NAFTA requires the development and implementation of an electronic funds transfer (EFT) system for the collection of certain depository taxes. This regulation implements the Electronic Federal Tax Payment System (EFTPS) by prescribing rules for financial institutions and Federal Reserve Banks that use EFT mechanisms to process Federal tax payments through the EFTPS. The EFTPS began operation in the fall of 1996.

This regulation also updates the rules governing the changes to the Treasury's investment program that were necessitated by the implementation of this EFT system.

EFFECTIVE DATE: March 5, 1998.

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SUPPLEMENTARY INFORMATION:**Background**

This regulation is authorized by the North American Free Trade Agreement Implementation Act (NAFTA), Public Law 103-182, Section 523, 107 Stat. 2057, 2161 (1993), the substantive provisions of which are codified at 26 U.S.C. 6302(h). NAFTA mandates that the Secretary of the Treasury (Secretary) phase-in the collection of a minimum percentage of certain types of depository

taxes by electronic funds transfer (EFT) and develop and implement an EFT system for the collection of such taxes. The Secretary has delegated responsibility to the Internal Revenue Service (IRS) for the former and to the Financial Management Service (FMS) for the latter. With the enactment of NAFTA, the FMS achieved its longstanding goal to collect depository taxes electronically. This regulation implements the FMS' Electronic Federal Tax Payment System (EFTPS), which began operation on October 28, 1996.

On September 30, 1996, the FMS published in the **Federal Register** a notice of proposed rulemaking (NPRM) that would govern the deposit of Federal taxes using EFT mechanisms (61 FR 51186). The NPRM also proposed rules updating Treasury's investment program to reflect the impact of the new electronic system. The original closing date for the submission of comments was November 21, 1996. However, the FMS published a notice in the **Federal Register** extending that date to January 13, 1997 (61 FR 59211).

Comments on the Proposed Rule

The title of this part has been changed in two steps for two reasons. The first change from "Treasury Tax and Loan Depositories" to the NPRM designation as "Treasury Tax and Loan Depositories and the Payment of Federal Taxes" reflects the importance of the addition of the EFTPS. Secondly, the title used in this Final Rule reverses the order in the NPRM title to shift the emphasis from the Treasury Tax and Loan (TT&L) depositories to the payment of Federal taxes through the EFTPS because under this Final Rule at § 203.9, "a financial institution does not need to be designated as a TT&L depository in order to process electronic Federal tax payments."

Two sections of the NPRM, §§ 203.4 and 203.5, have been combined in this Final Rule as § 203.4 causing all sections of the Final Rule after § 203.4 to be renumbered. For clarity, each section citation in this Final Rule is identified as either an NPRM or Final Rule citation. For example, the NPRM § 203.11 was the section covering Enrollment. All references to the NPRM section on Enrollment will identify it as NPRM § 203.11 (emphasis added). In the Final Rule, the section covering Enrollment is § 203.10. Therefore, all references to the Enrollment section of the Final Rule will identify it as § 203.10 in the *Final Rule* (emphasis added).

By the close of the January 13, 1997, comment period, the FMS received comments on the NPRM from twelve

organizations: six financial institutions and six industry trade associations. The following includes a discussion of the significant and most heavily commented upon issues:

Conformance With Industry Automated Clearing House (ACH) Rules

Commenters expressed concern with certain NPRM provisions that would require financial institutions to adhere to a set of rules different from private industry ACH rules. Eleven of the twelve commenters advocated the adoption of the National Automated Clearing House Association (NACHA) Operating Rules for ACH processing, enrollment, compensation, and/or credit reversals for electronic Federal tax payments.

Currently, the FMS is proposing a revision of 31 CFR Part 210 which considers adoption of NACHA rules wherever practicable. The revision as proposed would address the role of NACHA rules in all Federal payments and collections made through the ACH system. However, as the examples that follow illustrate, Part 203 requires certain exceptions to the wholesale adoption of industry rules due to EFTPS program considerations. Therefore, ACH entries governed by Part 203 are not subject to any provisions of Part 210 that are inconsistent with Part 203.

The FMS understands the commenters' interest in having a uniform set of rules governing both commercial and Federal transactions and has recognized these concerns by revising this Final Rule to conform with commercial operating rules to the extent practicable. For example, the FMS has revised the Final Rule to conform to commercial operating rules for both ACH credit reversals and the waiting period between the origination of a prenotification entry and the first payment.

However, Treasury, as an executive agency within the Federal Government, is constrained from the wholesale adoption of commercial operating rules. For example, the Internal Revenue Code provisions governing the disclosure of returns and return information preclude Treasury from adopting the commercial operating rules for electronic enrollments. In addition, the FMS is constrained from adopting commercial operating rules that would require Treasury to pay interest for payments erroneously made by financial institutions. Specifically, such interest is not recoverable from the United States unless expressly provided by statute. The FMS has not identified any statute that would authorize Treasury to pay such interest.

Enrollment and Enrollment Liabilities

Section 203.11(a) of the NPRM provided that the taxpayer may enroll in EFTPS using either a paper-based or electronic enrollment method. Section 203.11(b)(2) of the NPRM allowed a financial institution to assist its customers by offering electronic enrollment. However, even if the financial institution offered electronic enrollment, a representative of the financial institution would have to verify and sign an enrollment form, and provide a paper copy of the completed form to the taxpayer for the taxpayer's signature and submission to the Treasury Financial Agent (TFA).

Five commenters were concerned that no details were provided on how an electronic enrollment process would work and recommended that the FMS adopt procedures developed by NACHA to transmit enrollment data through the ACH using the standard entry class code, "ENR." One commenter suggested enrolling taxpayers through the EFTPS home page on the Internet. Additionally, five commenters questioned the need for a paper copy of the enrollment form to be submitted to the TFA when an electronic enrollment option is used. One commenter further recommended that the FMS send back an acknowledgment file including an acknowledgment number that could take the place of the taxpayer's written signature.

Section 203.10 of the Final Rule deletes all references to electronic enrollments since such electronic processes would not eliminate the IRS' need for a paper copy of an enrollment form signed by the taxpayer. Currently, the IRS requires the taxpayer's written signature for all enrollments in EFTPS. The written taxpayer signature provides the IRS with the requisite authority to disclose to the TFAs and to the taxpayer's financial institution the confidential taxpayer return information necessary to effect enrollment and payment transactions, provides the TFAs with the authority to initiate debits to the taxpayer's account, and provides the IRS with authority to resolve issues related to enrollments and payments. Until an all electronic enrollment process becomes feasible for IRS tax payments, taxpayers will continue to enroll in the EFTPS by means of paper enrollment forms.

Notwithstanding the deletion of the hybrid electronic/paper enrollment process from this Final Rule, the FMS understands that the IRS is undertaking efforts towards accepting electronic signatures. Treasury also will continue to work with entities such as NACHA to

determine the feasibility of using the ENR enrollment standard entry class code for EFTPS enrollments, and may look at other options for an all electronic enrollment process in the future.

NPRM § 203.11(c) provided that if a taxpayer enrolled for the ACH debit method, "* * * an authorized representative of the financial institution shall verify the accuracy of the financial institution routing number, taxpayer account number, and taxpayer account type * * * [and] shall sign the enrollment form attesting to the accuracy of the financial institution information."

Five commenters suggested that it is unnecessary and inappropriate for Treasury to require a financial institution to sign the enrollment form to verify bank routing and account numbers. The commenters stated that there is no way to verify that the signature is an authorized signature of a bank representative and that the banking information would be verified in the prenotification process. Another commenter supported the requirement for financial institutions to sign the enrollment form since it provides taxpayers with an opportunity to talk to their financial institutions and to ask questions.

The FMS agrees with both sets of comments, and has balanced both interests in the Final Rule. Specifically, § 203.10(c) of the Final Rule deletes the requirement that a financial institution sign the enrollment form, but requires the financial institution to verify certain information upon the specific request of the taxpayer. A financial institution may perform such verification by telephone.

One commenter requested additional information on the status of an enrollment if the form is not signed by a representative of the taxpayer's financial institution, and asked what, if any, liability is assumed by the financial institution if the form is unsigned or signed with inaccurate information. Because the Final Rule deletes the requirement that an authorized financial institution representative sign the enrollment form, such enrollment forms will be processed without a financial institution signature, and the financial institutions will not accrue any liabilities if authorized representatives do not sign such forms. However, the FMS may hold such financial institutions liable under § 203.14(a) of the Final Rule if taxpayers request verification of banking data, and the financial institutions fail to identify incorrect banking data that result in a late tax payment.

One commenter recommended that Treasury modify the enrollment form to require a taxpayer to obtain the signature of a financial institution representative as evidence of permission to use ACH credit origination services to make EFTPS payments. The FMS recognizes the importance of a taxpayer discussing the provision of ACH credit services with its financial institution before the taxpayer sends the enrollment form. Accordingly, the FMS has revised the enrollment form to instruct taxpayers electing the ACH credit option to verify in advance whether the financial institution is capable of providing ACH credit origination services.

One commenter inquired whether a taxpayer could enroll via a prenotification entry. The prenotification entry cannot be used to enroll a taxpayer because it does not provide all the required information. Taxpayers must enroll as prescribed in § 203.10 of the Final Rule.

Prenotification

NPRM § 203.13(b)(1) required financial institutions that receive an ACH debit entry to "timely verify the information contained in the ACH prenotification entry." Three commenters sought clarification on what information the financial institution is required to verify in the prenotification or zero dollar entry it receives. One financial institution commenter asked whether financial institutions must verify the taxpayer identification number (TIN). Section 203.12(b)(1) of the Final Rule clarifies that financial institutions need to verify the account number and account type, and not the TIN. Moreover, because the TFAs will not originate zero dollar entries, financial institutions will need to verify only information in prenotification entries.

NPRM § 203.13(c)(1) provided that the financial institution "shall originate an ACH credit prenotification entry that may be in the form of a zero dollar entry" and that credit entries may not be initiated less than 10 calendar days after the date the prenotification was transmitted. Some commenters expressed a preference for prenotification entries and some expressed a preference for zero dollar entries. Two commenters opposed the mandatory use of prenotification entries, and one favored it. Several commenters pointed out that the NACHA rules make prenotification entries optional. They noted that it would require computer system modifications to identify Federal tax payments in several situations: where a

file could contain Federal tax payments among many other types of payments, and where the credits are triggered by customers themselves. Nine commenters were critical of the 10 calendar day waiting period between origination of a prenotification or zero dollar entry and the first payment. Several pointed out that the NACHA rules were changed in March, 1997, to require a six business day waiting period between prenotification entries and the first payment.

The FMS recognizes the merits of these comments and has revised the Final Rule. Specifically, § 203.12(c)(1) of the Final Rule clarifies that the FMS will accept either an ACH prenotification entry containing the TIN in the entry detail record (no addenda) or the zero dollar entry with the TIN in the addenda record. The TFA will use the information to verify with the IRS that the TIN is valid and corresponds with an enrolled taxpayer. The FMS has limited the requirement that financial institutions originate prenotification entries for ACH credits. Under the Final Rule, a prenotification or zero dollar entry is not required unless specifically requested by the taxpayer. Financial institutions should note, however, that guidance sent from the TFAs following enrollment suggests that taxpayers instruct their financial institutions to originate zero dollar transactions or prenotification entries prior to the first payment. Consequently, financial institutions will have to be able to originate such entries. The FMS also has deleted the 10 calendar day waiting period between the origination of a prenotification entry and the first payment in light of the NACHA rules.

Prenotification Liabilities

The FMS received a number of inquiries regarding what liability, if any, is assumed by financial institutions in the prenotification process. In the context of ACH debits, the TFA will initiate a prenotification, not a zero dollar entry, for each taxpayer enrolling for ACH debit. Sections 203.12(b)(1) and (2) of the Final Rule require the financial institution receiving an EFTPS prenotification to "timely verify the account number and account type contained in the ACH prenotification entry [and] timely and properly return a prenotification entry that contains an invalid account number or account type, or is otherwise erroneous or unprocessable." In addition, § 203.14(a) in the Final Rule clarifies NPRM § 203.15(a) by providing that the FMS may assess interest where a financial institution failed to respond to an ACH prenotification entry as required in

§§ 203.12(b) and 203.12(c) of the Final Rule, where such failure resulted in a late tax payment. In the context of ACH credits, the FMS may hold a financial institution liable under § 203.14(a) of the Final Rule if a late tax payment results from the financial institution's failure to initiate a taxpayer-requested prenotification or zero dollar entry.

The FMS believes that the potential imposition of such liabilities on financial institutions during the prenotification process is fair, equitable, and a logical outgrowth of the NPRM. Specifically, the preamble to the NPRM notified readers that the liability provisions generally were geared towards placing liability for errors on the party making the errors. The FMS believes that this principle serves two important purposes here. First, it is an incentive for financial institutions to process EFTPS payments in accordance with this Part, which will help ensure that depository taxes are credited to the TGA on tax due date. Second, it makes the United States whole for the lost value of funds resulting from late tax payments. For example, a financial institution receiving an ACH debit prenotification entry may have little or no incentive to review and return timely a prenotification entry containing an invalid account number if it can do so without any financial exposure.

Acknowledgments

NPRM § 203.13(c)(4) required financial institutions originating ACH credit tax payments to provide a transaction trace number to their customers upon request. One commenter stated that the process for assigning and providing a trace number is unclear and the numbers provided by financial institution proprietary systems may not be sufficient.

The intent of this provision was to ensure that taxpayers have the means to trace their tax payments at the IRS if there is some discrepancy or problem. For example, in originating ACH credit entries, financial institutions transmit to the IRS transaction trace numbers, that are included in the IRS master file. If there is a question between the IRS and the taxpayer as to the timeliness of a tax payment, the taxpayer may obtain the transaction trace number from its financial institution, and provide it to the IRS, which will then trace the payment. The FMS seeks to protect the interests of taxpayers by ensuring that they have a means of tracing their tax payments while at the same time affording financial institutions maximum flexibility in providing taxpayers with the means to do so. Accordingly, § 203.12(c)(4) of the Final Rule requires financial institutions to

provide their customers, upon request, either transaction trace numbers or some other method to trace the tax payment.

Four commenters recommended that Treasury implement a system to provide electronic acknowledgments for ACH credit tax payments and three commenters recommended that Treasury utilize the new ACH acknowledgments ("ACK" and "ATX") developed by NACHA. The FMS currently is considering the operational implications of developing and utilizing the new NACHA acknowledgments.

Two of the commenters expressed concern over a perceived system bias between the ACH debit and the ACH credit acknowledgment process. The FMS believes that there is no system bias, and that taxpayers can easily obtain ACH acknowledgment numbers for both ACH debit and credit transactions. Specifically, EFTPS provides a taxpayer initiating an ACH debit through the telephone or personal computer with an automated response acknowledgment number at the end of the reporting session. Taxpayers initiating an ACH credit transaction may obtain an ACH credit acknowledgment number by placing a toll-free call to the EFTPS Customer Service Centers on the tax due date.

ACH credit deadlines

NPRM § 203.13(c)(3) and the preamble to the NPRM left open the possibility of a deadline different from that currently required for ACH credit entries. In the preamble to the NPRM, the FMS suggested that if a different ACH credit deadline were required, that deadline would be approximately 11:00 p.m. on the day before the entry was to settle. All of the commenters suggested that establishing an ACH credit deadline for EFTPS payments that is different from the standard deadline already in place for such entries would impose significant operational problems for financial institutions and/or confuse taxpayers/customers. The commenters were concerned that financial institutions would be unaware that ACH files originated by its customers would contain such tax payment credit entries subject to an earlier deadline. Several commenters suggested that the establishment of a separate deadline for EFTPS ACH credit payments may serve as a disincentive for financial institutions to offer such services to their taxpaying customers.

Section 203.12(c)(3) of the Final Rule remains substantively unchanged. The FMS needs the flexibility to change ACH credit deadlines for purposes of maximizing the timely investment of tax

receipts. However, the FMS emphasizes that it has no current plans to impose a deadline different from the existing standard ACH processing schedules. Moreover, the FMS would ensure that financial institutions are provided with sufficient advance notice of any deadline changes so that they may undertake any necessary steps to continue to process timely ACH credit entries on behalf of their customers. While the FMS recognizes the possibility that any deadline change may cause some financial institutions to cease offering such services to their customers, the FMS believes that the marketplace would fill any void.

ACH Credit Reversals

NPRM § 203.13(d) required advance IRS approval for all corrections of ACH credit entries. In general, the commenters opposed obtaining approval from the IRS for reversals of ACH credit entries, remarking that obtaining approval from IRS is cumbersome; the requests must be done manually and quickly; and that IRS could not respond quickly enough to prevent financial institutions from losing the value of funds. Several commenters suggested that the reversals be governed by NACHA rules, which at that time did not require ACH credit originators to notify receivers when initiating an ACH credit reversal.

The FMS recognizes the merits of these comments, and has revised the Final Rule. Specifically, § 203.12(d) of the Final Rule eliminates the need to obtain advance approval from the IRS before originating an ACH credit reversal. A December 1997 NACHA rule change requires an ACH originator to notify a receiver when making a reversing entry to the receiver's account. For the reasons stated above, the Final Rule does not require that IRS be notified when an ACH credit reversal is initiated. However, financial institutions are reminded of ACH record retention rules, and need to be able to provide documentation per the requirements of the procedural instructions.

Same-day payments

NPRM § 203.14(a) proposed a 2:00 P.M. FRB head office local zone time (LZT) deadline for all three same-day tax payment methods (Fedwire value, Fedwire non-value, and Direct Access). One commenter requested that the Fedwire deadline for Federal tax payments be the same as the normal Fedwire national deadline currently established for third party transactions (6:00 p.m. ET).

The FMS believes that a uniform same-day payment cutoff time is

necessary to maximize and meet the needs of Treasury's investment program. Under this program, Treasury invests tax payments with the taxpayers' financial institutions in open-ended interest-bearing obligations or "note balances." In order for these financial institutions to receive these investments, Treasury must designate and employ them separately as Treasury Tax and Loan (TT&L) note depositaries. The 2:00 p.m. LZT cutoff time is necessary to ensure that EFTPS tax payments transmitted by these financial institutions via Fedwire non-value and Direct Access are credited to their TT&L note balances on the same day, thereby maximizing Treasury's investment opportunities. Specifically, Fedwire non-value and Direct Access transactions are settled through the Federal Reserve's TT&L system. The 2:00 p.m. LZT cutoff is necessary to provide time for the TT&L system to process these two non-value transactions, and create the investment entries to credit the note depositaries' balances.

The FMS has decided to apply this same cutoff time to the Fedwire value payment method because it is in the interest of the Treasury's investment program that Fedwire value not be favored over the Fedwire non-value and Direct Access options. Specifically, tax payments remitted via the Fedwire value method are credited to Treasury's General Account at the FRB and cannot be invested with note option depositaries that day, thereby delaying Treasury's investment opportunities. If the cutoff time for the Fedwire value payment method was later than for the two non-value payment methods, informal conversations with financial institutions and the TFAs indicate that Fedwire value likely would be favored over the Fedwire non-value and Direct Access payment methods which would have detrimental effects on the Treasury's investment program.

Consequently, the FMS has decided to retain the 2:00 p.m. LZT cutoff time for all three same day payment methods. However, §§ 203.13(a), (e)(1)(i), and (e)(3) of the Final Rule delete specific references to this cutoff time, and instead refer to the procedural instructions that will contain the 2:00 p.m. LZT cutoff time.

Furthermore, the FMS currently is contemplating the adoption of a uniform national cutoff time of 5:00 p.m. Eastern Time (ET) for all same-day payments with a potential implementation date of mid-1999. The possibility of a uniform cutoff time stems from the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, Public Law 103-328, 108 Stat. 2338 (1994). Under this

law, a financial institution will have a single Federal Reserve account where its master account is located. The location of this master account will determine the cutoff time for all same-day Federal tax payments. If the FMS maintains the 2:00 p.m. LZT cutoff time, financial institutions with a master account located on the West Coast would enjoy a competitive advantage in attracting customers over financial institutions with a master account on the East Coast due to the additional three hours for making a same-day Federal tax payment. In order to prevent unfair business advantages among financial institutions, the FMS is considering an FRB recommendation to implement a uniform national cutoff time of 5:00 p.m. ET for all same-day payments. If the FMS decides to adopt such a uniform national cutoff time, the FMS will ensure that financial institutions will be provided adequate advance notice to make any necessary system changes.

In the preamble to the NPRM, the FMS requested comments on restricting the use of the Fedwire non-value and Direct Access same-day payment methods to TT&L note depositaries. One commenter supported FMS' underlying intent and five commenters opposed such restrictions. The FMS has decided against imposing any restrictions, and all three same-day mechanisms are available for use by any financial institution capable of originating these transactions.

Two commenters expressed concern over limiting the use of same-day payment mechanisms to certain categories of taxpayers. This Final Rule does not prescribe which payment methods taxpayers must use.

NPRM §§ 203.14(b), (c), and (d) provided that upon the request of the taxpayer, the taxpayer's financial institution shall provide the taxpayer with reference numbers for same-day transactions (the Input Message Accountability Data (IMAD) number and the Electronic Tax Application (ETA) reference number). For example, for Fedwire transactions, the ETA reference number is assigned once the payment has been received by the Federal Reserve's ETA. This number is provided to the TFAs and the IRS at the end of each business day and is available to originating financial institutions from their local FRB upon request only. Taxpayers wishing to receive the IMAD or ETA reference numbers on a day subsequent to the transaction date also may obtain such reference numbers by contacting the EFTPS Customer Service Centers. One

commenter suggested that the IMAD and ETA reference numbers for same-day payments should be provided to the taxpayer automatically.

The FMS does not accept this comment, and as a result, §§ 203.13(b), (c), and (d) of the Final Rule remain substantively unchanged. The FMS has weighed the needs of the taxpayers in receiving such reference numbers against the burdens that would be imposed upon financial institutions if the Final Rule were to require financial institutions to provide taxpayers with such numbers automatically. This Final Rule balances the needs of both parties by requiring financial institutions to provide their customers with such reference numbers upon the specific request of their customers. The FMS believes that to mandate that financial institutions provide their customers with these reference numbers in instances where the customer may not seek such numbers would be unduly burdensome on financial institutions given certain operational constraints. Taxpayers seeking such reference numbers on a continuous basis should tailor their contracts with their financial institutions to meet their needs.

NPRM § 203.14(e) defined the circumstances in which the FRB or the IRS could reverse or cancel a same-day payment. Two commenters recommended that taxpayers be contacted before the FRB or the IRS cancel or reject a same-day payment.

The FMS does not accept these comments. Therefore, section 203.13(e) of the Final Rule remains substantively unchanged. Due to the time critical nature of the same-day payment mechanism, it is neither feasible nor practicable to notify the taxpayer before a same-day payment is reversed or canceled. Specifically, all same-day payments are edited by the FRB's ETA, which will automatically reverse same-day tax payments that are late, e.g., that are received after the ETA deadline, or that are timely but do not contain enough information to identify the taxpayer. The FRB also reverses same-day payments at the direction of the IRS, which may direct a reversal in situations where a payment cannot be posted in the IRS database because the TIN is invalid, or where a taxpayer or financial institution have requested the funds be returned because of an overpayment. The FRB also may reverse or cancel tax payments at the request of the originating financial institution if the request is received prior to the ETA cutoff time on the transaction date.

In all cases, the FMS believes that it is the responsibility of financial institutions to notify their customers if

same-day payments are returned or canceled. This is especially important where timely same-day payments are returned or canceled so that customers may attempt to correct the payment prior to the cutoff time.

Interest Assessments for Lost Value of Funds

NPRM § 203.12(c) provided that Treasury will not pay interest on any payments erroneously paid to Treasury and subsequently refunded to the financial institution. Several commenters asked that Treasury compensate financial institutions for the time value of funds held.

The FMS rejects these comments, and, as a result, section 203.11(c) of the Final Rule remains substantively unchanged. It is a well settled principle that interest is not payable by the United States unless expressly provided by statute or in a contract authorized by law. This principle extends equally to situations where notions of equity would seem to militate in favor of the United States paying interest. Congress has expressly authorized the payment of interest for tax refunds when the IRS pays without being sued and when a taxpayer receives a judgment from a court for any overpayment of internal revenue taxes. See 26 U.S.C. 6402 and 28 U.S.C. 2411 respectively.

Because the FMS has not identified any statutory provision that authorizes it to pay interest to financial institutions that make erroneous payments that subsequently are refunded by Treasury, the FMS is unable to compensate financial institutions for their lost value of funds.

NPRM § 203.15 set forth the circumstances and procedures for the assessment, calculation, and collection of interest from financial institutions for purposes of making the United States whole for the lost value of funds resulting from late tax payments. One commenter suggested that only taxpayers be held liable for late tax payments. Other commenters opposed the interest assessment provisions. One commenter recommended that financial institutions only be penalized if they transmit a certain number of late tax payments each year.

The FMS does not accept these comments, and § 203.14 of the Final Rule remains substantively unchanged on these points. The legislative scheme underlying EFTPS is to ensure that certain depository taxes are credited to the TGA on the tax due date. If an EFTPS tax payment is not credited to the TGA on the tax due date, the IRS will impose a penalty on the taxpayer pursuant to 26 U.S.C. 6656. However,

IRS Revenue Ruling 94-46 (July 6, 1994) provides that the IRS will abate this penalty if the taxpayer establishes that the instructions the taxpayer provided to its financial institution were timely and correct, and that it had sufficient funds to make the tax payment. For example, the FMS understands that if the taxpayer did everything right in initiating an ACH credit payment, but the taxpayer's financial institution failed to originate the payment timely, which resulted in a late tax payment, the IRS will abate the penalty imposed upon the taxpayer. However, under these circumstances, the United States will have lost the value of funds from the date the taxpayer specified that its payment should settle to the TGA to the time the late tax payment actually settled to the TGA.

As a result, the FMS believes that to implement successfully the legislative scheme underlying EFTPS, it may be necessary in these circumstances to hold a financial institution liable for the lost value of funds. Specifically, if a financial institution is not held liable for its mistakes which result in a late tax payment, a financial institution may have less incentive to process timely such tax payments for credit to the TGA on the tax due date. The interest assessment in most instances simply recovers the imputed value of funds erroneously retained by the financial institution. The FMS further believes that financial institutions can minimize this risk by imposing conditions on their customers, and by initiating prenotification or zero dollar entries.

Nevertheless, the FMS will not assess interest on financial institutions for errors resulting in late tax payments where such errors occur before the effective date of this Final Rule.

Furthermore, § 203.14(b) of the Final Rule limits a financial institution's interest liability to seven calendar days for ACH debit transactions and 45 calendar days for both ACH credit and same-day payment transactions. The FMS has established this cap in recognition of the fact that taxpayers have a responsibility, upon learning of their financial institution's error, to initiate a new payment transaction. The seven calendar day cap for ACH debit transactions stems from the fact that if the taxpayer's financial institution returns the taxpayer's ACH debit transaction, the TFA will take immediate steps to mail the taxpayer a notification letter. The FMS believes that upon receipt of this letter from the TFA, the taxpayer has a responsibility to initiate a new tax payment transaction. The FMS also believes that this process generally should take no longer than

seven calendar days from the date the tax payment would have settled to the TGA. The 45 day cap for ACH credit and same-day payment transactions stems from the fact that if the TFA returns an ACH credit transaction or if the FRB returns a same-day payment transaction to the financial institution, the taxpayer, at the latest, will learn of the return upon receipt of its monthly statement of account from its financial institution. The 45 days is based upon an estimated 30 day statement cycle, and 15 days processing and mail time.

One commenter asked whether Treasury will assess interest on financial institutions when the late tax payment is due to the ACH operator, a system problem, a daylight overdraft, or other causes. Whether the FMS will assess interest on a financial institution to make the United States whole for the lost value of funds depends on the specific facts and circumstances. Financial institutions will have the right to contest any interest assessment under § 203.16 of the Final Rule.

Several commenters asked for more specific information on the interest assessment process. The specific procedures will be published in the procedural instructions in the Treasury Financial Manual (TFM).

NPRM § 203.15(c) provided that a financial institution that processes tax payments under this part is deemed to authorize the FRB, acting as Treasury's fiscal agent, to debit its reserve account for interest assessments. One commenter suggested that Treasury should not initiate a debit to a financial institution's reserve account. Another commenter suggested that Treasury give financial institutions an opportunity to appeal the interest prior to paying it.

The FMS does not accept these comments, and § 203.14(c) of the Final Rule remains substantively unchanged. The FMS believes that the operational steps underlying the collection of interest assessments will take several months from the date of the late tax payment due to the extensive IRS research required. Because the FMS will not assess "interest on interest," the FMS believes that affording a financial institution an opportunity to contest the assessment prior to collecting it only would exacerbate the lost value of funds to the United States, especially in light of the cap on a financial institution's liability at § 203.14(b) of the Final Rule. Moreover, § 203.14(c) of the Final Rule, which authorizes the FMS to debit the interest assessment from a financial institution's reserve account, is consistent with the current process by which FMS recovers the lost value of funds from financial institutions in the

paper Federal Tax Deposit (FTD) system. The FRB will send an electronic message to the financial institution the day prior to the day that the financial institution's reserve account is debited for the interest assessment.

NPRM § 203.15(d) and § 203.14(d) of the Final Rule provide that Treasury will not assess interest on a financial institution when the taxpayer has not satisfied the conditions imposed by its financial institution. Several commenters asked what information a financial institution would need to provide to establish that the taxpayer failed to meet the financial institution's conditions. The FMS has no pre-set requirements; however, the FMS will consider such information as the written conditions themselves; a saved electronic file; and/or a tape of telephonic instructions showing the time and the direction to initiate a transaction. The FMS will not regulate the agreements between the financial institution and its customers, and therefore, will not give guidance on the conditions a financial institution may impose.

One commenter asked if a financial institution must disclose to the taxpayer its proof that the taxpayer failed to satisfy its requirements for making an EFTPS payment. This part does not regulate the exchange of information between a taxpayer and its financial institution.

Unauthorized Debits

NPRM § 203.16 prohibited financial institutions from initiating debits to the TGA unless they had prior written permission. NPRM § 203.16 also provided that financial institutions that do initiate such unauthorized debit entries are liable for the amount of the debit and an interest charge at the Federal funds rate plus two percent, and are deemed to authorize the Federal Reserve Bank to debit their reserve accounts for the amount of the debit plus interest.

One commenter pointed out that a customer theoretically could initiate a debit to the TGA by using a customer delivery system, and that a financial institution would suffer an undue burden if it had to ensure that its customers could not initiate such debits. The FMS does not accept this comment, and § 203.15 of the Final Rule is substantively unchanged on this point. The FMS believes that financial institutions are responsible for how they allow their customers to key in transaction information. This approach is consistent with commercial operating rules, which generally provide that originating depository financial

institutions warrant that their entries are authorized by both the originator and the receiver.

However, should such a situation occur, the TFA will attempt to return the unauthorized debit entry in time for same-day settlement. If this return is made on the same day, there will be no need to recover the principal nor will there be any interest charge. If the return is not accomplished in the same day, the financial institution shall be liable to the Treasury for the amount of the transaction and interest charges calculated according to the procedural instructions published in the TFM.

One commenter stated that reversals should be excluded expressly from this section. The FMS agrees and has clarified § 203.15(a) of the Final Rule.

One commenter recommended that the interest charge assessed for an unauthorized ACH debit be lowered to the Federal funds rate. The FMS does not accept this comment and § 203.15(d) of the Final Rule remains substantively unchanged. This higher rate is intended to deter unauthorized debits from the TGA.

Appeal and Dispute Resolution

NPRM § 203.17 afforded financial institutions the opportunity to appeal an interest assessment under NPRM § 203.15 or an interest charge under NPRM § 203.16. Several commenters requested an explanation as to how this process would work. The FMS will provide greater detail on these processes in its procedural instructions in the TFM. Nevertheless, § 203.16 of the Final Rule expands the administrative remedies afforded financial institutions. Specifically, if a financial institution is unsuccessful in contesting an interest assessment, it may appeal the administrative denial to a higher level Treasury official. This two-step administrative review process is similar to the one currently used for the paper FTD system.

Compensation

NPRM § 203.19(a)(8) prohibited financial institutions serving as TT&L depositories from accepting compensation from taxpayers for handling the deposit of tax payments in the paper FTD system. Three commenters suggested that the FMS remove this prohibition. The FMS does not accept this comment and § 203.18 of the Final Rule is substantively unchanged. While the FMS believes that such comments may have merit, the NPRM did not give affected parties adequate notice of this possibility. As a result, the FMS is constrained from accepting these comments. However,

the FMS intends to issue an NPRM on removing this prohibition.

Two commenters noted that the NPRM was silent on whether financial institutions could charge taxpayers for processing tax payments under EFTPS. These commenters recommended that the FMS expressly authorize financial institutions to charge their customers for processing their EFTPS tax payments. The FMS does not accept these comments, and the Final Rule remains silent on whether financial institutions, acting as the taxpayers' agents, can charge their customers for processing EFTPS payments.

The decision not to regulate the fees financial institutions can charge under EFTPS stems from the fact that the EFTPS eliminates one of the benefits currently provided financial institutions under the paper-based FTD system. Specifically, when a taxpayer makes its tax payment under the FTD system, the tax payment is deposited into a non-interest-bearing TT&L account at the financial institution. The financial institution retains the imputed value of these funds until the next day when the funds either are credited to the TGA or are invested with the financial institution in interest-bearing notes. Under EFTPS, these tax payments will no longer be deposited overnight into such non-interest bearing accounts, and the financial institutions will no longer retain the value of these funds. The FMS believes that it is best left to the marketplace to decide what fees, if any, financial institutions will charge their customers. However, the FMS believes that any fees for ACH credit or debit entries will be insignificant.

Collateral

NPRM § 203.25(f)(1) was modeled on existing § 203.14(f)(1) and provided that in the event of a TT&L depository's insolvency or closure, Treasury may apply the collateral pledged to satisfy any claim of the United States. The NPRM preamble explained Treasury's longstanding interpretation that "any claim of the United States" includes, but is not limited to, claims arising out of the depository relationship for which the collateral was originally pledged. One commenter suggested that the TT&L collateral only be used to satisfy TT&L claims. The FMS does not accept this comment, and the FMS' interpretation of § 203.24(f)(1) of the Final Rule remains unchanged. The FMS believes that this interpretation is necessary to protect the United States from loss.

NPRM § 203.25 set forth Treasury's collateral security requirement for financial institutions serving as TT&L

depositories. One commenter asked how a TT&L depository would be notified of the amount in the Note Option/Direct Investment account so that it could deposit sufficient collateral to secure the deposits. This information appears in the daily Federal Reserve account activity statement, which the depository can access after 9:00 a.m. ET via Fedline by using the Accounting Services application and choosing the IAS Account Inquiry option or by using the TT&L application and choosing the Host Account Activity Report. Section 203.24 of the Final Rule provides that note option depositories that participate in the direct investment program are not required to collateralize continuously the pre-established maximum balance but must be prepared to pledge collateral on the day the direct investment is placed.

One commenter sought confirmation that same-day EFTPS payments initiated by a financial institution serving as a TT&L depository that miss the cutoff time are not required to be collateralized. The preamble of the NPRM stated that "financial institutions processing tax payments under the EFTPS . . . need not pledge collateral, unless they elect to participate in Treasury's investment program." EFTPS payments, including those that the depository is unable to complete, are not required to be collateralized.

Regulatory Analysis

These regulations are not a significant regulatory action as defined in Executive Order 12866. Accordingly, a regulatory assessment is not required. It is hereby certified that this revision will not have a significant economic impact on a substantial number of small entities. Therefore, a regulatory flexibility analysis is not required. This regulation will not impose significant costs on small entities. It is further expected that such costs associated with electronic tax payments will be offset by cost savings resulting from reductions in the paperwork burden and the availability of a user-friendly electronic tax collection system.

List of Subjects in 31 CFR Part 203

Banks, Banking, Electronic Funds Transfers, Taxes.

For the reasons set out in the preamble, 31 CFR part 203 is revised to read as follows:

PART 203—PAYMENT OF FEDERAL TAXES AND THE TREASURY TAX AND LOAN PROGRAM

Subpart A—General Information

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203.24 Collateral security requirements.

Authority: 12 U.S.C. 90, 265–266, 332, 391, 1452(d), 1464(k), 1767, 1789a, 2013, 2122, and 3102; 26 U.S.C. 6302; 31 U.S.C. 321, 323 and 3301–3304.

Subpart A—General Information

§ 203.1 Scope.

The regulations in this part govern the processing of Federal tax payments by financial institutions and the Federal Reserve Banks (FRB) using electronic payment or paper methods; the designation of Treasury Tax and Loan (TT&L) depositories; and the operation of the Department of the Treasury's (Treasury) investment program.

§ 203.2 Definitions.

As used in this part:

(a) *Advice of credit* means the Treasury form used in the Federal Tax

Deposit system that is supplied to depositories to summarize and report Federal tax deposits. The current form is Treasury Form 2284. Advice of credit information also may be delivered electronically.

(b) *Automated Clearing House (ACH) credit entry* means a transaction originated by a financial institution in accordance with applicable ACH formats and applicable laws, regulations, and procedural instructions.

(c) *Automated Clearing House (ACH) debit entry* means a transaction originated by a Treasury Financial Agent (TFA), in accordance with applicable ACH formats and applicable laws, regulations, and instructions.

(d) *Business day* means any day on which the FRB of the district is open.

(e) *Direct Access transaction* means same-day Federal tax payment information transmitted by a financial institution directly to the Electronic Tax Application at an FRB using the Fedline Taxpayer Deposit Application.

(f) *Direct investment* means placement of Treasury funds with a depository and a corresponding increase in a depository's note balance.

(g) *Electronic Federal Tax Payment System (EFTPS)* means the system through which taxpayers remit Federal tax payments electronically.

(h) *Electronic Tax Application (ETA)* means a sub-system of EFTPS that receives, processes, and transmits same-day Federal tax payment information for taxpayers. ETA activity is comprised of Fedwire value transfers, Fedwire non-value transactions, and Direct Access transactions.

(i) *Electronic Tax Application (ETA) reference number* means the unique number assigned to each ETA transaction by an FRB.

(j) *Federal funds rate* means the Federal funds rate published weekly by the Board of Governors of the Federal Reserve System.

(k) *Federal Reserve account* means an account with reserve or clearing balances held by a financial institution at an FRB.

(l) *Federal Reserve Bank of the district* means the FRB that services the geographical area in which the financial institution is located, or such other FRB that may be designated in an FRB operating circular.

(m) *Federal Tax Deposit (FTD)* means a tax deposit or payment made using an FTD coupon.

(n) *Federal Tax Deposit coupon (FTD coupon)* means a paper form supplied to a taxpayer by the Treasury for use in the FTD system to accompany deposits of

Federal taxes. The current paper form is Form 8109.

(o) *Federal Tax Deposit system (FTD system)* means the paper-based system through which taxpayers remit Federal tax payments by presenting an FTD coupon and payment to a depository or an FRB. The depository prepares an advice of credit summarizing all FTDs.

(p) *Federal taxes* means those Federal taxes or other payments specified by the Secretary of the Treasury as eligible for payment through the procedures prescribed in this part.

(q) *Fedwire* means the funds transfer system owned and operated by the FRBs.

(r) *Fedwire non-value transaction* means the same-day Federal tax payment information transmitted by a financial institution to an FRB using a Fedwire type 1090 message to authorize a payment.

(s) *Fedwire value transfer* means a Federal tax payment made by a financial institution using a Fedwire type 1000 message.

(t) *Financial institution* means any bank, savings bank, savings and loan association, credit union, or similar institution.

(u) *Fiscal Agent* means the Federal Reserve acting as agent for the Treasury.

(v) *Input Message Accountability Data (IMAD)* means a unique number assigned to each Fedwire transaction by the financial institution sending the transaction to an FRB.

(w) *Note option* means that program available to a TT&L depository under which Treasury invests in obligations of the depository. The amount of such investments will be evidenced by an open-ended interest-bearing note balance maintained at the FRB of the district.

(x) *Procedural instructions* means the procedures contained in the Treasury Financial Manual, Volume IV (IV TFM), other Treasury instructions issued through the TFAs, and FRB operating circulars issued consistent with this part.

(y) *Recognized insurance coverage* means the insurance provided by the Federal Deposit Insurance Corporation, the National Credit Union Administration, and by insurance organizations specifically qualified by the Secretary.

(z) *Remittance option* means that program available to a depository that processes FTD payments, under which the amount of deposits credited by the depository to the TT&L account will be withdrawn by the FRB for deposit to the Treasury General Account on the day that the FRB receives the advices of credit supporting such deposits.

(aa) *Same-day payment* means the following ETA payment options:

- (1) Direct Access transaction;
- (2) Fedwire non-value transaction;

and

- (3) Fedwire value transfer.

(bb) *Secretary* means the Secretary of the Treasury, or the Secretary's delegate.

(cc) *Special direct investment* means the placement of Treasury funds with a depository and a corresponding increase in a depository's note balance, where the investment specifically is identified as a "special direct investment" and may be secured by collateral retained in the possession of the depository pursuant to the terms of § 203.24(c)(2)(i).

(dd) *Tax due date* means the day on which a tax payment is due to Treasury, as determined by statute and Internal Revenue Service (IRS) regulations.

(ee) *Transaction trace number* means an identifying number assigned by the taxpayer's financial institution to each ACH credit transaction.

(ff) *Treasury Financial Agent (TFA)* means a financial institution designated as an agent of Treasury for processing EFTPS enrollments, receiving EFTPS tax payment information, and originating ACH debit entries on behalf of Treasury as authorized by the taxpayer.

(gg) *Treasury General Account (TGA)* means an account maintained in the name of the United States Treasury at an FRB.

(hh) *Treasury Tax and Loan (TT&L) account* means the Treasury account maintained by a depository in which funds are credited by the depository after receiving and collateralizing FTDs.

(ii) *Treasury Tax and Loan depository (depository)* means a financial institution designated as a depository by the FRB of the district for the purpose of maintaining a TT&L account and/or note balance.

(jj) *Treasury Tax and Loan (TT&L) Program* means the program for collecting Federal taxes and investing the Government's excess operating funds.

(kk) *Treasury Tax and Loan (TT&L) rate of interest* means the Federal funds rate less twenty-five basis points (i.e., $\frac{1}{4}$ of 1 percent).

§ 203.3 Financial institution eligibility for designation as a Treasury Tax and Loan depository.

(a) To be designated as a TT&L depository, a financial institution shall be insured as a national banking association, state bank, savings bank, savings and loan, building and loan, homestead association, Federal home loan bank, credit union, trust company,

or a U.S. branch of a foreign banking corporation, the establishment of which has been approved by the Comptroller of the Currency.

(b) A financial institution shall possess the authority to pledge collateral to secure TT&L account balances and/or a note balance.

(c) In order to be designated as a TT&L depository for the purposes of processing tax deposits in the FTD system, a financial institution shall possess under its charter either general or specific authority permitting the maintenance of the TT&L account, the balance of which is payable on demand without previous notice of intended withdrawal. In addition, note option depositories shall possess either general or specific authority permitting the maintenance of a note balance, which is payable on demand without previous notice of intended withdrawal.

§ 203.4 Designation of financial institutions as Treasury Tax and Loan depositories.

(a) *Parties to the agreement.* To be designated as a TT&L depository, a financial institution shall enter into a depository agreement with Treasury's fiscal agent, the FRB. By entering into this agreement, the financial institution agrees to be bound by this part, and procedural instructions issued pursuant to this part.

(b)(1) *Application procedures.* An eligible financial institution seeking designation as a depository and, thereby, the authority to maintain a TT&L account and/or a note balance shall file with the FRB, Financial Management Service Form 458, "Financial Institution Agreement and Application for Designation as a TT&L Depository," and Financial Management Service Form 459, "Resolution Authorizing the Financial Institution Agreement and Application for Designation as a TT&L Depository," certified by its board of directors. Financial Management Service Forms 458 and 459 are available upon request from the FRB of the district.

(2) Depositories processing tax payments in the FTD system are required to elect either the remittance or the note option.

(c) *Designation.* Each financial institution satisfying the eligibility requirements and the application procedures will receive from the FRB notification of its specific designation as a TT&L depository. A financial institution is not authorized to maintain a TT&L account or note balance until it has been designated as a TT&L depository by the FRB.

§ 203.5 Obligations of the depository.

A depository shall:

(a) Administer a note balance, if not participating in the FTD System.

(b) Administer a TT&L account and, if applicable, a note balance, if participating in the FTD System.

(c) Comply with the requirements of Section 202 of Executive Order 11246, entitled "Equal Employment Opportunity" (3 CFR, 1964-1965 Comp. p. 339) as amended by Executive Orders 11375 and 12086 (3 CFR, 1966-1970 Comp., p. 684; 3 CFR, 1978 Comp. p. 230), and the regulations issued thereunder at 41 CFR Chapter 60.

(d) Comply with the requirements of Section 503 of the Rehabilitation Act of 1973, as amended, and the regulations issued thereunder at 41 CFR part 60-741, requiring Federal contractors to take affirmative action to employ and advance in employment qualified individuals with disabilities.

(e) Comply with the requirements of Section 503 of the Vietnam Era Veterans' Readjustment Assistance Act of 1972, as amended, 38 U.S.C. 4212, Executive Order 11701 (3 CFR 1971-1975 Comp. p. 752), and the regulations issued thereunder at 41 CFR parts 60-250 and 61-250, requiring Federal contractors to take affirmative action to employ and advance in employment qualified special disabled veterans and Vietnam-era veterans.

§ 203.6 Compensation for services.

Except as provided in the procedural instructions, Treasury will not compensate financial institutions for servicing and maintaining the TT&L account, or for processing tax payments through the EFTPS or the FTD system.

§ 203.7 Termination of agreement or change of election or option.

(a) *Termination by Treasury.* The Secretary may terminate the agreement of a depository at any time upon notice to that effect to that depository, effective on the date set forth in the notice.

(b) *Termination or change of election or option by the depository.* A depository may terminate its depository agreement, or change its option or election, consistent with this part and the procedural instructions, by submitting notice to that effect in writing to the FRB effective at a prospective date set forth in the notice.

§ 203.8 Application of part and procedural instructions.

The terms of this part and procedural instructions issued pursuant to this part shall be binding on financial institutions that process tax payments and/or maintain a note balance under

this part. By accepting or originating Federal tax payments, the financial institution agrees to be bound by this part and by procedural instructions issued pursuant to this part.

Subpart B—Electronic Federal Tax Payments

§ 203.9 Scope of the subpart.

This subpart prescribes the rules by which financial institutions shall process Federal tax payment transactions electronically. A financial institution does not need to be designated as a TT&L depository in order to process electronic Federal tax payments. In addition, a financial institution that does process electronic Federal tax payments under this subpart does not thereby become a Federal Government depository and shall not advertise itself as one because of that fact.

§ 203.10 Enrollment.

(a) *General.* Taxpayers shall complete an enrollment process with the TFA prior to making their first electronic Federal tax payment.

(b) *Enrollment forms.* The TFA shall provide financial institutions and taxpayers with enrollment forms upon request. The taxpayer is responsible for completing the enrollment form, obtaining the verifications required on the form, and returning the enrollment form to the TFA.

(c) *Verification.* If the taxpayer elects the ACH debit entry method of paying taxes, an authorized representative of the financial institution shall verify the accuracy of the financial institution routing number, taxpayer account number, and taxpayer account type at the request of the taxpayer.

§ 203.11 Electronic payment methods.

(a) *General.* Electronic payment methods for Federal tax payments available under this subpart include ACH debit entries, ACH credit entries, and same-day payments. Any financial institution that is capable of originating and/or receiving transactions for these payment methods, by itself or through a correspondent financial institution, may do so on behalf of a taxpayer.

(b) *Conditions to making an electronic payment.* Nothing contained in this part shall affect the authority of financial institutions to enter into contracts with their customers regarding the terms and conditions for processing payments, provided that such terms and conditions are not inconsistent with this subpart and applicable law governing the particular transaction type.

(c) *Payment of interest for time value of funds held.* Treasury will not pay

interest on any payments erroneously paid to Treasury and subsequently refunded to the financial institution.

§ 203.12 Future-day reporting and payment mechanisms.

(a) *General.* A financial institution may receive an ACH debit entry, originated by the TFA at the direction of the taxpayer; or, a financial institution may originate an ACH credit entry, at the direction of the taxpayer. Taxpayers will be credited for the actual amount received by Treasury.

(b) *ACH debit.* A financial institution receiving an ACH debit entry originated by the TFA shall, as applicable:

(1) Timely verify the account number and account type contained in an ACH prenotification entry;

(2) Timely and properly return a prenotification entry that contains an invalid account number or account type, or otherwise is erroneous or unprocessable;

(3) Timely and accurately notify the TFA of incorrect information on entries received, using a Notification of Change entry; and

(4) Timely and accurately return an entry not posted, including but not limited to, a return or a contested dishonored return for acceptable return reasons, as set forth in the procedural instructions.

(c) *ACH credit.* A financial institution originating an ACH credit entry at the direction of a taxpayer shall:

(1) At the request of the taxpayer, originate either an ACH prenotification containing the taxpayer's identification number or a zero dollar ACH entry with the appropriate addenda record. Additional format information is contained in the procedural instructions;

(2) Format the ACH credit entry in the ACH format approved by Treasury for Federal tax payments;

(3) Originate an ACH credit entry by the appropriate deadline, as specified by the FRB or Treasury, whichever is earlier, in order to meet the tax due date specified by the taxpayer; and

(4) Provide the taxpayer, upon request, a transaction trace number, or some other method to trace the tax payment.

(d) *ACH credit reversals.* Reversals may be initiated for a duplicate or erroneous file or entry. No advance approval from, or notification to, the IRS is required when originating an ACH credit reversal. Documentation of reversals shall be made available as set forth in the procedural instructions.

§ 203.13 Same-day reporting and payment mechanisms.

(a) *General.* A financial institution or its authorized correspondent may initiate same-day reporting and payment transactions on behalf of taxpayers. A same-day payment must be received by the FRB of the district by the deadline established by the Treasury in the procedural instructions. Taxpayers will be credited for the actual amount received by Treasury.

(b) *Fedwire value transfer.* To initiate a Fedwire value tax payment, the financial institution shall be a Fedwire participant and shall comply with the FRB's Fedwire format for tax payments. The taxpayer's financial institution shall provide the taxpayer, upon request, the IMAD and the ETA reference numbers for a Fedwire value transfer. The financial institution may obtain the ETA reference number for Fedwire value transfers from its FRB by supplying the related IMAD number. Fedwire value transfers settle immediately to the TGA and thus are not credited to a depository's note balance.

(c) *Fedwire non-value transaction.* By initiating a Fedwire non-value transaction, a financial institution authorizes the FRB of the district to debit its Federal Reserve account or, for a TT&L depository, to debit the Federal Reserve account of the depository or its designated correspondent financial institution, for the amount of the tax payment specified in the transaction. To initiate a Fedwire non-value transaction, the financial institution shall be a Fedwire participant and shall comply with the FRB's Fedwire format for tax payments. The taxpayer's financial institution shall provide the taxpayer, upon request, the IMAD and ETA reference numbers for the Fedwire non-value transaction. The financial institution may obtain the ETA reference number for Fedwire non-value transactions from its FRB by supplying the related IMAD number.

(1) For a note option depository using a Fedwire non-value transaction, the tax payment amount will be credited to the depository's note balance on the day of the transaction.

(2) For a remittance option depository using a Fedwire non-value transaction, the tax payment amount will be debited from the Federal Reserve account of the depository or the depository's designated correspondent and credited to the TGA on the day of the transaction.

(3) For a non-TT&L depository financial institution using a Fedwire non-value transaction, the tax payment amount will be debited from the financial institution's Federal Reserve

account and credited to the TGA on the day of the transaction.

(d) *Direct Access Transaction.* By initiating a Direct Access transaction, a financial institution authorizes the FRB of the district to debit its Federal Reserve account or, for a TT&L depository, to debit the Federal Reserve account of the depository or its designated correspondent financial institution for the amount of the tax payment specified in the transaction. The taxpayer's financial institution shall provide the taxpayer, upon request, the ETA reference number for the Direct Access transaction.

(1) For a note option depository using a Direct Access transaction, the tax payment amount will be credited to the depository's note balance on the day of the transaction.

(2) For a remittance option depository or a non-TT&L depository financial institution using a Direct Access transaction, the tax payment amount will be debited from the Federal Reserve account of the financial institution or its designated correspondent financial institution, and credited to the TGA on the day of the transaction.

(e) *Cancellations and reversals.* In addition to cancellations due to insufficient funds in the financial institution's Federal Reserve account, the FRB may reverse a same-day transaction:

(1) If the transaction:

(i) Is originated by a financial institution after the deadline established by the Treasury in the procedural instructions;

(ii) Has an unenrolled taxpayer identification number; or

(iii) Does not meet the edit and format requirements set forth in the procedural instructions; or,

(2) At the direction of the IRS, for the following reasons:

(i) Incorrect taxpayer name;

(ii) Overpayment; or

(iii) Unidentified payment; or,

(3) At the request of the financial institution that sent the same-day transaction, if the request is made prior to the deadline established by Treasury in the procedural instructions on the day the payment was made.

(f) Other than as stated in paragraph (e) of this section, Treasury is not obligated to reverse all or any part of a payment.

§ 203.14 Electronic Federal Tax Payment System interest assessments.

(a) *Circumstances subject to interest assessments.* Treasury may assess interest on a financial institution in instances where a taxpayer that failed to meet a tax due date proves to the IRS

that the delivery of tax payment instructions to the financial institution was timely and that the taxpayer satisfied the conditions imposed by the financial institution pursuant to § 203.11(b). Treasury also may assess interest where a financial institution failed to respond to an ACH prenotification entry on an ACH debit as required in § 203.12(b) or failed to originate an ACH prenotification or zero dollar entry on an ACH credit as described in § 203.12(c) which then resulted in a late payment.

(b) *Calculation of interest assessment.* Any interest assessed under this section will be at the TT&L rate. The interest will be assessed from the day the taxpayer specified that its payment should settle to the Treasury until the receipt of the payment by Treasury, subject to the following limitations: For ACH debit transactions, interest will be limited to no more than seven calendar days; for ACH credit and same-day transactions, interest will be limited to no more than 45 calendar days. The limitation of liability in this paragraph does not apply to any interest assessment in which there is an indication of fraud, the presentation of a false claim, or misrepresentation or embezzlement on the part of the financial institution or any employee or agent of the financial institution.

(c) *Authorization to assess interest.* A financial institution that processes Federal tax payments made by electronic payment methods under this subpart is deemed to authorize the FRB to debit its Federal Reserve account or the account of its designated correspondent financial institution for any interest assessed under this section. Upon the direction of Treasury, the FRB shall debit the Federal Reserve account of the financial institution or the account of its designated correspondent financial institution for the amount of the assessed interest.

(d)(1) *Circumstances not subject to the assessment of interest.* (1) Treasury will not assess interest on a taxpayer's financial institution if a taxpayer fails to meet a tax due date because the taxpayer has not satisfied conditions imposed by the financial institution pursuant to § 203.11(b) and the financial institution has not contributed to the delay. The burden is on the financial institution to establish, pursuant to the procedures in § 203.16, that the taxpayer has not satisfied the conditions and that the financial institution has not contributed to the delay.

(2) Treasury will not assess interest on a financial institution if the delay causing the interest assessment is due to the FRB or the TFA and the financial

institution did not contribute to the delay. The burden is on the financial institution to establish, pursuant to the procedures in § 203.16, that it did not cause or contribute to the delay.

§ 203.15 Prohibited debits through the Automated Clearing House.

(a) *General.* The Treasury has instituted operational safeguards to scrutinize all entries that remove funds from the TGA. In the event funds are removed from the TGA without authority, this section sets forth the liability of financial institutions originating such entries. Accordingly, a financial institution shall not originate an ACH transaction to debit the TGA without the prior written permission of Treasury. Unauthorized entries under this section do not include reversal entries of previously initiated ACH credits authorized in § 203.12(d).

(b) *Liability.* A financial institution that originates an unauthorized ACH entry that debits the TGA shall be liable to Treasury for the amount of the transaction and shall be liable for interest charges as specified in paragraph (d) of this section.

(c) *Authorization to recover principal and assess interest charge.* By initiating unauthorized debits to the TGA through the ACH, a financial institution is deemed to authorize the FRB to debit its Federal Reserve account or the account of its designated correspondent financial institution for any principal and, if applicable, an interest charge assessed by Treasury under this section.

(d) *Interest charge calculation.* The interest charge shall be at a rate equal to the Federal funds rate plus two percent. The interest charge shall be assessed for each calendar day from the day the TGA was debited to the day the TGA is recredited with the full amount of principal due.

§ 203.16 Appeal and dispute resolution.

(a) *Contest.* A financial institution may contest any interest assessed under § 203.14, any principal or interest assessed under § 203.15, or any late fees assessed under § 203.20. The financial institution shall submit information supporting its position and the relief sought. The information must be received, in writing, by the Treasury officer or fiscal agent identified in the procedural instructions, no later than 90 calendar days after the date the FRB debits the reserve account of the financial institution under §§ 203.14, 203.15, or 203.20. The Treasury officer or fiscal agent will: uphold the assessment, or reverse the assessment, or modify the assessment, or mandate other action.

(b) *Appeal.* The financial institution may appeal the decision to Treasury as set forth in the procedural instructions. No further administrative review of the Treasury's decision is available under this Part.

(c) *Recoveries.* In the event of an over or under recovery of either interest, principal, or late fees, Treasury will instruct the FRB to credit or debit the Federal Reserve account of the financial institution or its designated correspondent financial institution, as appropriate.

Subpart C—Federal Tax Deposits

§ 203.17 Scope of the subpart.

This subpart applies to all depositories that accept FTD coupons and governs the acceptance and processing of those coupons.

§ 203.18 Tax deposits using Federal Tax Deposit coupons.

(a) *FTD coupons.* A depository that accepts FTD coupons, through any of its offices that accept demand and/or savings deposits, shall:

(1) Accept from a taxpayer, cash, a postal money order drawn to the order of the depository, or a check or draft drawn on and to the order of the depository, covering an amount to be deposited as Federal taxes when accompanied by an FTD coupon on which the amount of the deposit has been properly entered in the space provided. A depository may accept, at its discretion, a check drawn on another financial institution, but it does so at its option and absorbs for its own account any float and other costs involved.

(2) Issue a counter receipt when requested to do so by a taxpayer that makes an FTD deposit over the counter.

(3) Place a stamp impression on the face of each FTD coupon in the space provided. The stamp shall reflect the date on which the tax deposit was received and the name and location of the depository. The timeliness of the tax payment will be determined by reference to the date stamped by the depository on the FTD coupon.

(4) Credit, on the date of receipt, all FTD deposits to the TT&L account and administer that account pursuant to the provisions of this part.

(5) Forward, each day, to the IRS Center servicing the geographical area in which the depository is located, the FTD coupons for all FTD deposits received that day. The FTD coupons shall be accompanied by an advice of credit reflecting the total amount of all FTD coupons.

(6) Establish an adequate record of all FTD deposits prior to transmittal to the

IRS Center so that the depository will be able to identify deposits in the event tax deposit coupons are lost in shipment. For tracking purposes, a record shall be made of each FTD deposit showing, at a minimum, the date of deposit, the taxpayer identification number, and the amount of the deposit. The depository's copy of the advice of credit may be used to provide the necessary information if individual deposits are listed separately, showing date, taxpayer identification number, and amount.

(7) Deliver its advices of credit to the FRB by the cutoff hour designated by the FRB for receipt of advices.

(8) Not accept compensation from taxpayers for accepting FTDs and handling them as required by this section.

(b) *FTD deposits with Federal Reserve Banks.* An FRB shall:

(1) Accept an FTD directly from a taxpayer when such tax deposit is:

(i) Mailed or delivered by a taxpayer; and

(ii) Provided in the form of cash or a check or postal money order payable to the order of that FRB; and,

(iii) Accompanied by an FTD coupon on which the amount of the tax deposit has been properly entered in the space provided.

(2) Issue a counter receipt, when requested to do so by a taxpayer that makes an FTD over the counter; and,

(3) Place, in the space provided on the face of each FTD coupon accepted directly from a taxpayer, a stamp impression reflecting the name of the FRB and the date on which the tax deposit will be credited to the TGA. Timeliness of the Federal tax payment will be determined by this date.

However, if a deposit is mailed to an FRB, it shall be subject to the "Timely mailing treated as timely filing and paying" clause of the Internal Revenue Code, 26 U.S.C. 7502; and,

(4) Credit the TGA with the amount of the tax payment;

(i) On the date the payment is received, if payment is made in cash; or,

(ii) On the date the proceeds of the tax payment are collected, if payment is made by postal money order or check.

§ 203.19 Note option.

(a) *Late delivery of advices of credit.* If an advice of credit does not arrive at the FRB before the designated cutoff hour for receipt of such advices, the FRB will post the funds to the note balance as of the next business day after the date on the advice of credit. This is the date on which funds will begin to earn interest for Treasury.

(b) *Transfer of funds from TT&L account to the note balance.* For a

depository selecting the note option, funds equivalent to the amount of deposits credited by a depository to the TT&L account shall be withdrawn by the depository and credited to the note balance on the business day following the receipt of the tax payment.

§ 203.20 Remittance option.

(a) *FTD late fee.* If an advice of credit does not arrive at the FRB before the designated cutoff hour for receipt of such advices, an FTD late fee in the form of interest at the TT&L rate will be assessed for each day's delay in receipt of such advice. Upon the direction of Treasury, the FRB shall debit the Federal Reserve account of the financial institution or the account of its designated correspondent financial institution for the amount of the late fee.

(b) *Withdrawals.* For a depository selecting the Remittance Option, the amount of deposits credited by a depository to the TT&L account will be withdrawn upon receipt by the FRB of the advices of credit. The FRB will charge the depository's Federal Reserve account or the account of the depository's designated correspondent financial institution.

Subpart D—Investment Program and Collateral Security Requirements for Treasury Tax and Loan Depositories

§ 203.21 Scope of the subpart.

This subpart provides rules for TT&L depositories on crediting note balances under the various payment methods; debiting note balances; and pledging collateral security.

§ 203.22 Sources of balances.

Depositories electing to participate in the investment program can receive Treasury's investments in obligations of the depository from the following sources:

(a) FTDs that have been credited to the TT&L account pursuant to subpart C of this part;

(b) EFTPS ACH credit and debit transactions, Fedwire non-value transactions, and Direct Access transactions pursuant to subpart B of this part; and

(c) Direct investments and special direct investments pursuant to subpart D of this part.

§ 203.23 Note balance.

(a) *Additions.* Treasury will invest funds in obligations of depositories selecting the note option. Such obligations shall be in the form of open-ended, interest-bearing notes; and additions and reductions will be reflected on the books of the FRB of the district.

(1) *FTD system.* A depository processing tax deposits using the FTD system and electing the note option shall debit the TT&L account and credit its note balance as stated in § 203.19(b).

(2) EFTPS.

(i) *ACH debit and ACH credit.* A note option depository processing EFTPS ACH debit entries and/or ACH credit entries shall credit its note balance for the value of the transactions on the date that an exchange of funds is reflected on the books of the Federal Reserve Bank of the district. Financial institutions may refer to the procedural instructions for information on how to ascertain the amount of the credit to the note balance.

(ii) *Fedwire non-value and Direct Access.* A note option depository processing Fedwire non-value and/or Direct Access transactions pursuant to subpart B of this part shall credit its note balance and debit its customer's account for the value of the transactions on the date ETA receives and processes the transactions.

(b) *Other additions.* Other funds from Treasury may be offered from time to time to certain note option depositories through direct investments, special direct investments, or other investment programs.

(c) *Note balance withdrawals.* The amount of the note balance shall be payable on demand without prior notice. Calls for payment on the note will be by direction of the Secretary through the FRBs. On behalf of Treasury, the FRB shall charge the reserve account of the depository or the depository's designated correspondent on the day specified in the call for payment.

(d) *Interest.* A note shall bear interest at the TT&L rate. Such interest is payable by a charge to the Federal Reserve account of the depository or its designated correspondent in the manner prescribed in the procedural instructions.

(e) Maximum balance.

(1) *Note option depositories.* A depository selecting the note option shall establish a maximum balance for its note by providing notice to that effect in writing to the FRB of the district. The maximum balance is the amount of funds for which a note option depository is willing to provide collateral in accordance with § 203.24(c)(1). The depository shall provide the advance notice required in the procedural instructions before reducing the established maximum balance unless it is a reduction resulting from a collateral re-evaluation as determined by the depository's FRB. That portion of any advice of credit or EFTPS tax payment, which, when

posted at the FRB, would cause the note balance to exceed the maximum balance amount specified by the depositary, will be withdrawn by the FRB that day.

(2) *Direct investment depositaries.* A note option depositary that participates in direct investment shall set a maximum balance for direct investment purposes which is higher than its peak balance normally generated by the depositary's advices of credit and EFTPS tax payment inflow. The direct investment note option depositary shall provide the advance notice required in the procedural instructions before reducing the established maximum balance.

(3) *Special direct investment depositaries.* Special direct investments, while credited to the note balance, shall not be considered in setting the amount of the maximum balance or in determining the amounts to be withdrawn where a depositary's maximum balance is exceeded.

§ 203.24 Collateral security requirements.

Financial institutions that process EFTPS tax payments, but are not TT&L depositaries, have no collateral requirements under this part. Financial institutions that are note option depositaries or remittance option depositaries have collateral security requirements, as follows:

(a) *Note option.*

(1) *FTD deposits and EFTPS tax payments.* A depositary shall pledge collateral security in accordance with the requirements of paragraphs (c)(1), (d), and (e) of this section in an amount that is sufficient to cover the pre-established maximum balance for the note, and, if applicable, the closing balance in the TT&L account which exceeds recognized insurance coverage. Depositaries shall pledge collateral for the full amount of the maximum balance at the time the maximum balance is established. If the depositary maintains a TT&L account, the depositary shall pledge collateral security before crediting deposits to the TT&L account.

(2) *Direct investments.* A note option depositary that participates in direct investment is not required to pledge collateral continuously in the amount of the pre-established maximum balance. However, each note option depositary participating in direct investment shall pledge, no later than the day the direct investment is placed, the additional collateral in accordance with paragraphs (c)(1), (d), and (e) of this section to cover the total note balance including those funds received through direct investment. If a direct investment depositary has a history of frequent

collateral deficiencies, it shall fully collateralize its maximum balance at all times.

(3) *Special direct investments.* Before special direct investments are credited to a depositary's note balance, the note option depositary shall pledge collateral security, in accordance with the requirements of paragraphs (c)(2) and (e) of this section, to cover 100 percent of the amount of the special direct investments to be received.

(b) *Remittance option.* Prior to crediting FTD deposits to the TT&L account, a remittance option depositary shall pledge collateral security in accordance with the requirements of paragraph (c)(1), (d), and (e) of this section in an amount which is sufficient to cover the balance in the TT&L account at the close of business each day, less recognized insurance coverage.

(c) *Deposits of securities.*

(1) Collateral security required under paragraphs (a)(1), (2), and (b) of this section shall be deposited with the FRB of the district, or with a custodian or custodians within the United States designated by the FRB, under terms and conditions prescribed by the FRB.

(2)(i) Collateral security required under paragraph (a)(3) of this section shall be pledged under a written security agreement on a form provided by the FRB of the district. The collateral security pledged to satisfy the requirements of paragraph (a)(3) of this section may remain in the pledging depositary's possession and the fact that it has been pledged shall be evidenced by advices of custody to be incorporated by reference in the written security agreement. The written security agreement and all advices of custody covering collateral security pledged under that agreement shall be provided by the depositary to the FRB of the district. Collateral security pledged under the agreement shall not be substituted for or released without the advance approval of the FRB of the district, and any collateral security subject to the security agreement shall remain so subject until an approved substitution is made. No substitution or release shall be approved until an advice of custody containing the description required by the written security agreement is received by the FRB of the district.

(ii) Treasury's security interest in collateral security pledged by a depositary in accordance with paragraph (c)(2)(i) of this section to secure special direct investments is perfected without Treasury taking possession of the collateral security for a period not to exceed 21 calendar days

from the day of the depositary's receipt of the special direct investment.

(d) *Acceptable securities.* Unless otherwise specified by the Secretary, collateral security pledged under this section may be transferable securities, owned by the depositary free and clear of all liens, charges, or claims, of any of the classes listed in the procedural instructions. Collateral values will be assigned by the FRB of the district.

(e) *Assignment of securities.* A TT&L depositary that pledges acceptable securities which are not negotiable without its endorsement or assignment may furnish, in lieu of placing its unqualified endorsement on each security, an appropriate resolution and irrevocable power of attorney authorizing the FRB to assign the securities. The resolution and power of attorney shall conform to such terms and conditions as the FRB shall prescribe.

(f) *Effecting payments of principal and interest on securities pledged as collateral.*

(1) *General.* If the depositary fails to pay, when due, the whole or any part of the funds received by it for credit to the TT&L account, and/or if applicable, its note balance; or otherwise violates or fails to perform any of the terms of this part, or fails to pay when due amounts owed to the United States or the United States Treasury; or if the depositary is closed for business by regulatory action or by proper corporate action, or in the event that a receiver, conservator, liquidator or any other officer is appointed; then the Treasury, without notice or demand, may sell, or otherwise collect the proceeds of all or part of the collateral, including additions and substitutions; and apply the proceeds, to satisfy any claims of the United States against the depositary. All principal and interest payments on any security pledged to protect the note balance (if applicable) and/or the TT&L account (if applicable), due as of the date of the insolvency or closure, or thereafter becoming due, shall be held separate and apart from any other assets and shall constitute a part of the pledged security available to satisfy any claim of the United States.

(2) *Payment procedures.*

(i) Subject to the waiver in paragraph (f)(2)(iii) of this section, each depositary (including, with respect to such depositary, an assignee for the benefit of creditors, a trustee in bankruptcy, or a receiver in equity) shall immediately remit each payment of principal and/or interest received by it with respect to collateral pledged pursuant to this section to the FRB of the district, as fiscal agent of the United States, and in

any event shall so remit no later than 10 days after receipt of such a payment.

(ii) Subject to the waiver in paragraph (f)(2)(iii) of this section, each obligor on a security pledged by a depository pursuant to this section, upon notification that the Treasury is entitled to any payment associated with that pledged security, shall make each payment of principal and/or interest

due with respect to such security directly to the FRB of the district, as fiscal agent of the United States.

(iii) The requirements of paragraphs (f)(2)(i) and (ii) of this section are hereby waived for only so long as a pledging depository avoids both termination from the program under § 203.7; and also, those circumstances identified in paragraph (f)(1) which may lead to the

collection of the proceeds of collateral or the waiver is otherwise terminated by Treasury.

Dated: January 27, 1998.

Richard L. Gregg,

Acting Commissioner.

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