

Common Check Complications

Agenda

- Late Returns
- Altered Checks
- Forged/Counterfeit Checks
- Forged Indorsement



Exceptions - Returns

- Return items may be directed back to:
 - BOFD, or
 - Prior collecting or presenting bank
- Returns processes dependent on channel used and agreements in place
 - Must still follow regulatory requirements
 - For expeditious return, check must be received at depository bank by 2:00 pm 2nd business day following banking day of presentment
- Reg CC requires Paying Bank:
 - Identify return **and** reason for return
 - Clearly indicate reason for return
 - If substitute check, place information within image on front of substitute check

Adjustments – By Agreement

Federal Reserve Operating Circular 3 (OC3)

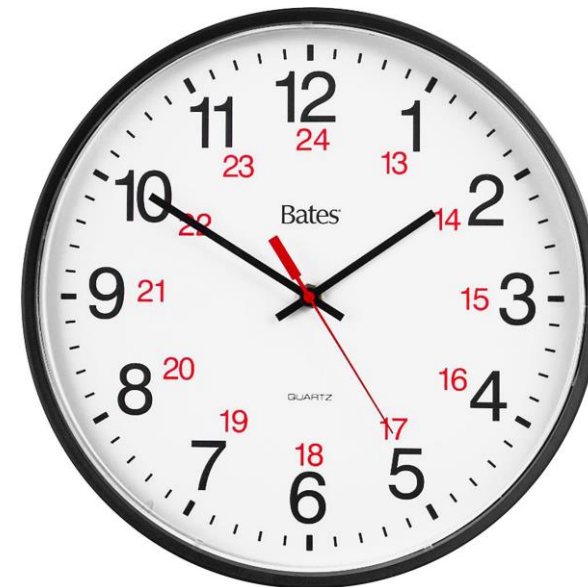
- FRBs “Check Adjustments Quick Reference Guide” provides:
 - Reporting timeframe
 - Requirements for adjustment request through FRB
- Outlines specific adjustment types, related timing, documentation (DTF) requirements, etc.

ECCHO Adjustment Rules and Matrix

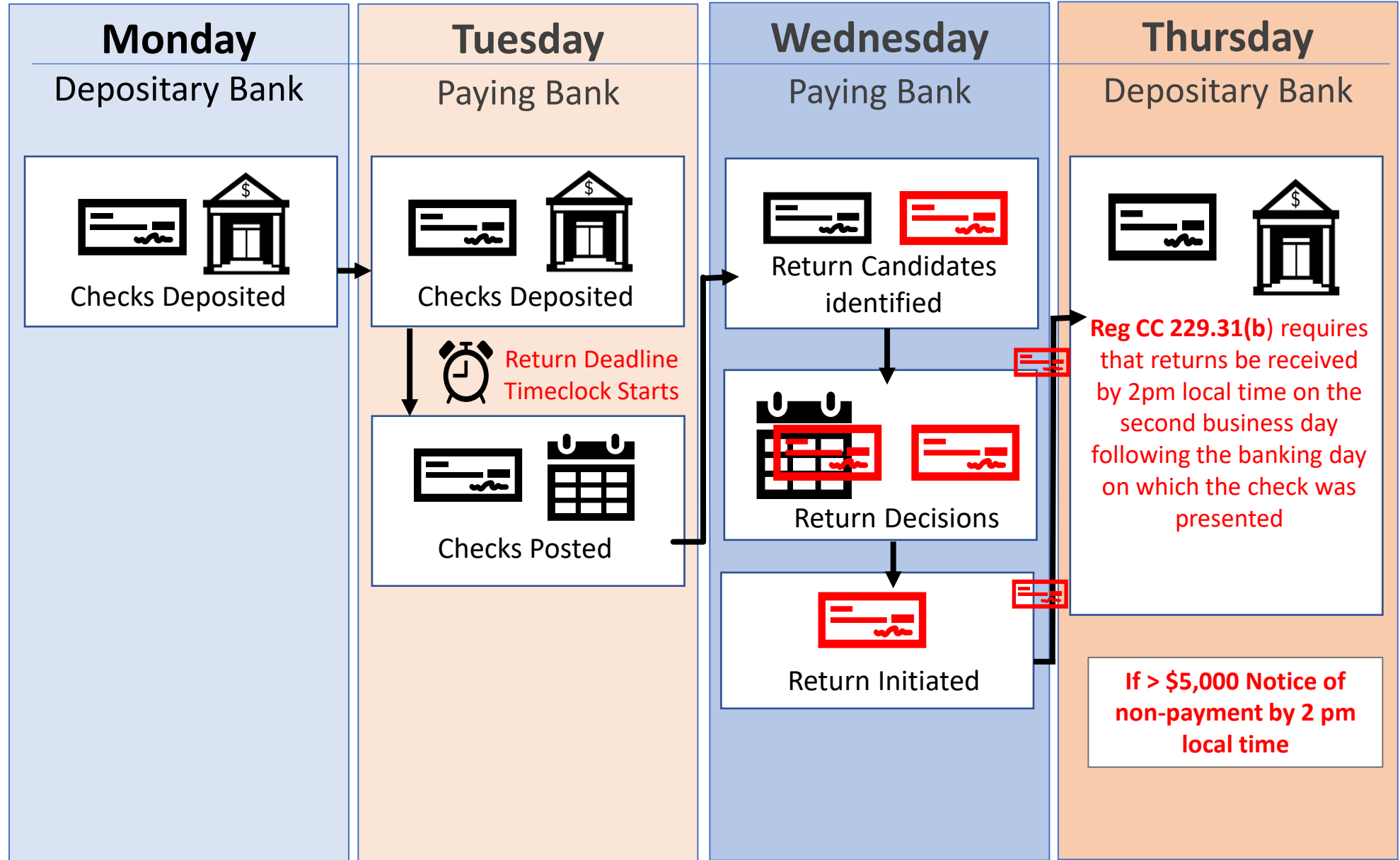
- Apply to Members for image exchange/return activities
 - Whether or not forward or return item exchanged under ECCHO Rules

Returns - Timeframe

- UCC = requires you make the determination to pay or dishonor the item by midnight of the day following presentment
- Reg CC = requires items to be returned, to be handled expeditiously
 - Return must reach depository bank by 2:00 p.m. (local time) two days after presentment

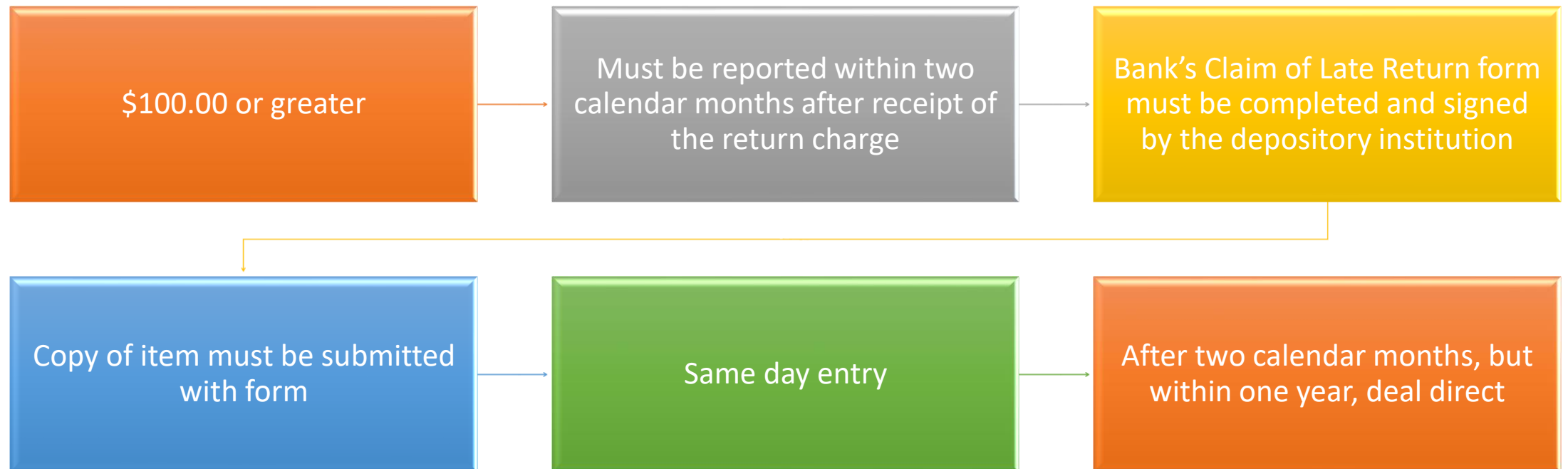


Return Deadlines



Late Return Claims - FRB

Current process for handling late returns



Duty to Report

UCC 4-406 Customer's Duty to Discover and Report Unauthorized Signature or Alteration

(c) If a bank sends or makes available a statement of account or items pursuant to subsection (a), the customer must exercise **reasonable promptness** in examining the statement or the items to determine whether any payment was not authorized because of an alteration of an item or because a purported signature by or on behalf of the customer was not authorized.

(f)...a customer who does not within **one year** after the statement...discover and report the customer's unauthorized signature or any alteration on the item is precluded from asserting against the bank the unauthorized signature or alteration

UCC Transfer Warranties

Person or collecting bank transferring item warrants to the transferee and any subsequent transferee

Entitled to enforce the item

All signatures on the item are authentic and authorized

Item has not been altered

Item is not subject to a defense or claim

Warrantor has no knowledge of any insolvency proceeding with respect to the maker

For remotely created consumer item, person on whose account the item is drawn authorized item and amount for which it is drawn

UCC Presentment Warranties

- Person presenting item and every previous transferor warrants to the drawee
 - Entitled to enforce draft
 - Or authorized to obtain payment / acceptance of draft on behalf of a person entitled to enforce the draft
 - Item has not been altered
 - **Warrantor has no knowledge that signature of the purported drawer of the draft is unauthorized**
 - For remotely created consumer item, person on whose account the item is drawn authorized item and amount for which it is drawn

Alterations UCC 3-407 – Definition

- An unauthorized change in an instrument that purports to modify in any respect the obligation of a party, or an unauthorized addition of words or numbers or other change to an incomplete instrument relating to the obligation of a party
 - Changing the payee name or changing number or relations of parties
 - Any increase or reduction in amount
 - Backdating date of a postdated check
 - Completing an incomplete check other than as authorized
 - Any other unauthorized addition or deletion which would change contract between parties

Alterations – General Rules

Paying Bank is liable to its account holder for paying altered check

- Unless maker is negligent, ratifies transaction, or is precluded from asserting claim;
- Unless check is paid according to its original (unaltered) terms, or for an incomplete check altered by unauthorized completion, according to its terms as completed

Depository Bank is responsible for the loss

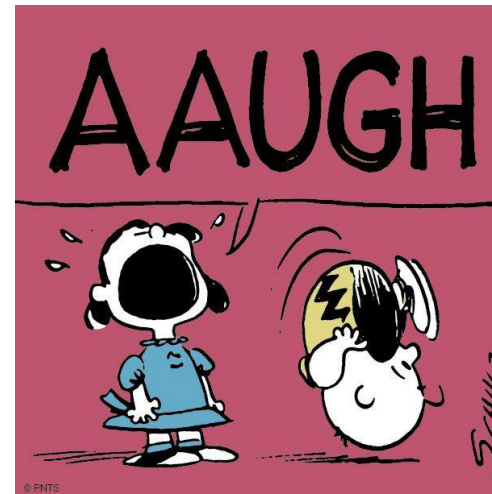
- Warrants to Paying Bank check has not been altered

Depositor is liable to Depository Bank for damages arising from alteration

- Based on account/deposit agreement

Altered Check Scenario

Charlie wrote a check to Lucy for \$500. Linus saw the check in the mailbox and through check washing, changed the name of the payee from Lucy to himself. Linus took the check to his bank and deposited the check. Lucy called Charlie three weeks later to yell at him for not sending the check. Charlie was confused, as he can see the check cleared his account two weeks ago.



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Altered Check

- Loss & Liability:
 - Depository Bank (Linus's bank) is responsible for the loss
 - Warrants to Paying Bank (Charlie's bank) check has not been altered
 - Depositor is liable to Depository Bank
 - Paying Bank is responsible for the loss if:
 - Drawer's signature does not match the signature card
 - Paying Bank is liable to its account holder for paying an altered check

Altered Check

- Resolution:
 - Paying Bank:
 - If timely, return as altered, no affidavit required
 - If after return timeframe, deal direct with BOFD
 - Obtain an affidavit from account holder (Charlie)
 - Send a breach of warranty claim letter with copy of the check and affidavit
 - Depository Bank:
 - If timely return, accept return and charge back to depositor (Linus)
 - If deal direct claim is received:
 - Reimburse Paying Bank if check has been altered
 - Deny claim if check contains an unauthorized drawer's signature

Forged Signature/Counterfeit Check

Forged drawer/maker signature

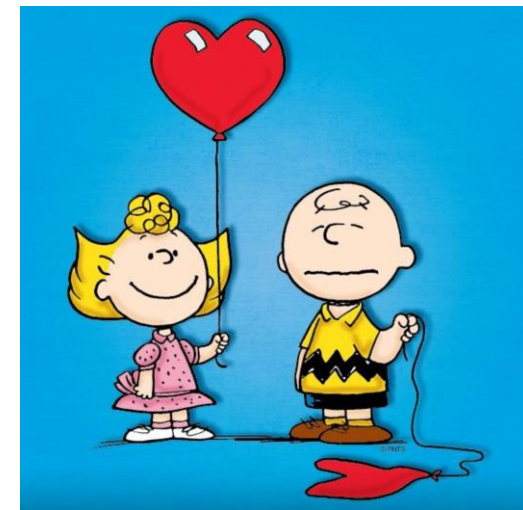
- Unauthorized signature under UCC

Counterfeit Check

- Printed with names and addresses of legitimate financial institutions.
- Even though the bank and account and routing numbers may be real they can still be a fake

Forged Signature/Counterfeit Check Scenario

Sally sees Charlie's checkbook sitting on the kitchen table. She doesn't think Charlie will notice a missing check, and she is pretty good at forging his signature. She takes a check, writes it payable to herself for \$500, signs Charlie's name, and deposits it into her bank account. Charlie calls his bank when his debit card doesn't work because of a low balance, and discovers this check that he never wrote.



Forged/Counterfeit Check

- Loss & Liability:
 - Depository Bank (Sally's bank) is not liable
 - Warrants to Paying Bank they had no knowledge the drawer's signature was unauthorized
 - If ECCHO Rule 9 applies, Depository Bank liable to the extent funds are available in the depositor's account
 - Paying Bank (Charlie's bank) is liable to its account holder for paying an unauthorized draft
 - Drawer's signature does not match the signature card

Forged/Counterfeit Check

- Resolution:
 - Credit customer back in the amount of unauthorized check
 - Send a Hold Harmless letter to Depository Bank requesting return of funds
 - If both financial institutions are ECCHO members, submit a Rule 9 claim
 - Both FIs must not be opted out of Rule 9

Forged Indorsement

Check is payable to multiple parties

- One party forges the indorsements of all payees and negotiates the check
- Check payable to a merchant or consumer
 - Check stolen and payee indorsement forged to negotiate the check

Breach of UCC Transfer & Presentment warranties

- Person transferring and/or presenting the item for payment is “entitled to enforce” the item
- Liability lies with the Bank of First Deposit

Forged Indorsement Scenario

Charlie wrote a check to Lucy for \$500. Linus saw the check in the mailbox, took it and signed Lucy's name on the back of the check. Linus took the check to his bank and deposited the check in his account. Lucy called Charlie three weeks later to yell at him for not sending the check. Charlie was again confused, as he can see the check cleared his account two weeks ago.



Forged Indorsement

- Rules that Apply:
 - UCC: Transfer & Presentment Warranties (UCC 4-207 & 4-208)
 - The Depository Bank warrants:
 - It is entitled to enforce the draft or authorized to obtain payment or acceptance of the draft on behalf of a person entitled to enforce the draft
 - All signatures on the item are authentic and authorized

Forged Indorsement

- Loss & Liability:
 - Depository Bank is liable to the Paying Bank for a forged indorsement
 - BOFD is in the best position to verify the payee's identity/signature
 - The Depositor is liable to the Depository Bank

Forged Indorsement

- Resolution:
 - Paying Bank:
 - Obtain an affidavit from the account holder or payee (either Charlie or Lucy)
 - Send a breach of warranty claim letter to BOFD with copy of check and affidavit
 - Depository Bank:
 - Reimburse Paying Bank if check contains a forged payee signature or is deposited into an account other than that of named payee
 - Deny claim if check was deposited into named payee's account



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