

Check Brainteasers

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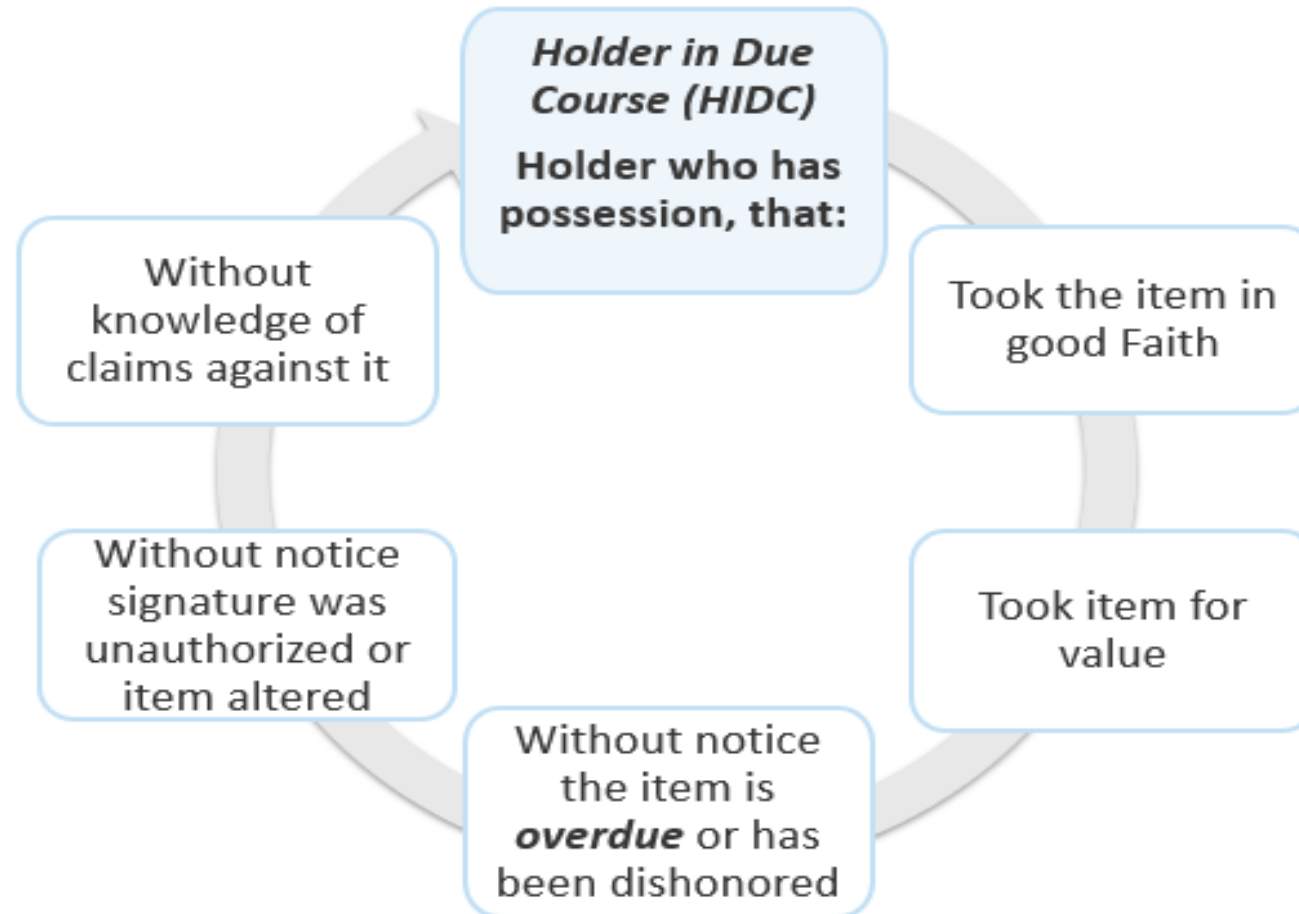
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Agenda

- Holder in Due Course
- RDC Indemnity
- Electronically Created Item (ECI)
- Remotely Created Check (RCC)
- Claim of Damage Due to Under-encoding
- Stop Payments

Holder and Holder in Due Course



What are the benefits to being a HIDC?

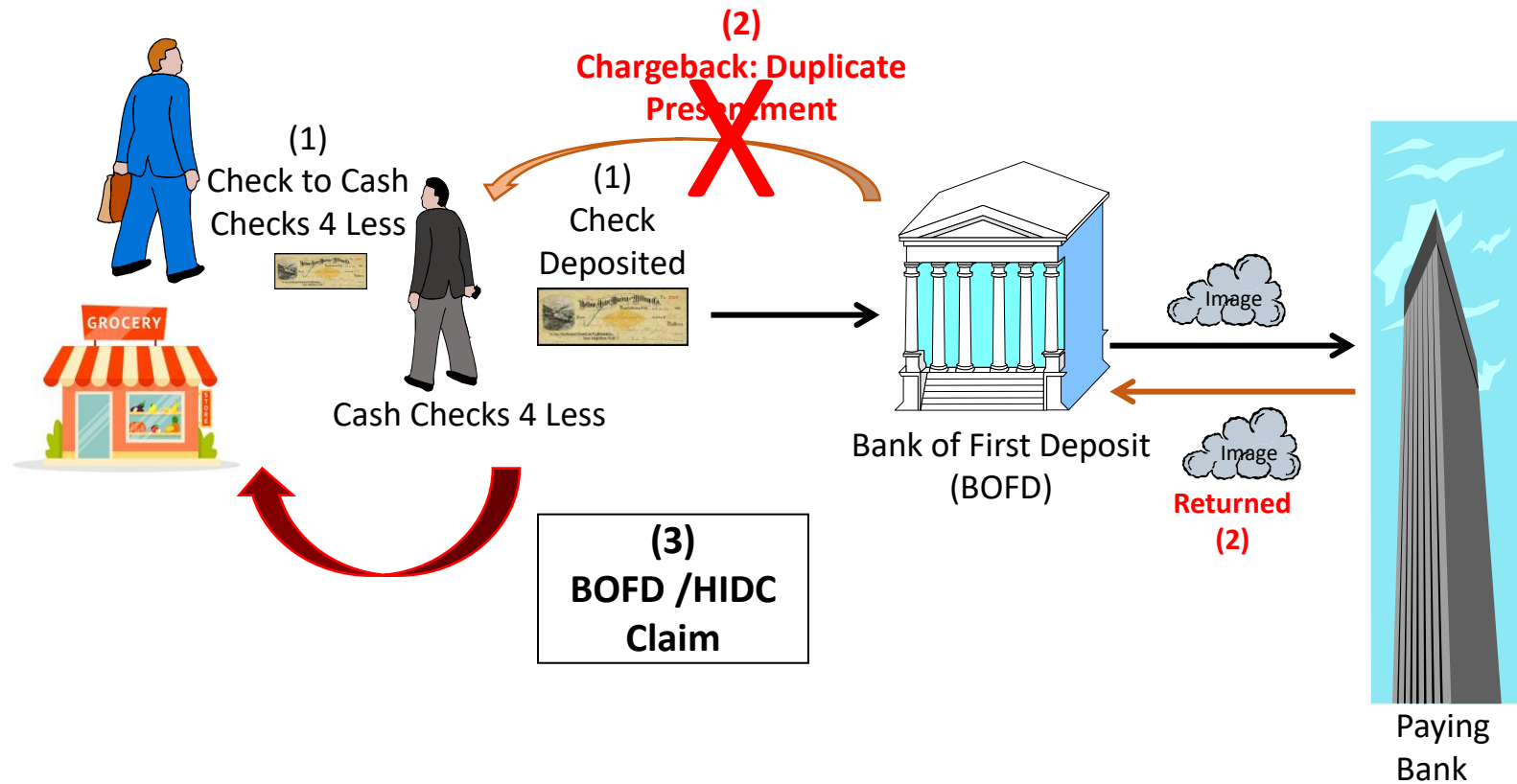
- Can enforce item against Drawer
- Can make a claim to the person who signed the check and ordered payment (Drawer)
 - Even if that check was returned unpaid by the Drawer's bank (Paying Bank)
 - Financial intermediary, such as Depository Bank (BOFD) or Collecting Bank should not be affected by disputes between the Drawer and Payee of check regarding the underlying transaction

Holder in Due Course Scenario

Guy's Grocery Store issued a check to one of their employees and the employee deposited the check via mobile RDC on 2/20/24. The employee (payee) then took the check to Cash Checks 4 Less and received cash for it. Cash Checks 4 Less presented the check and it was flagged as a duplicate and returned on 2/21/24. Cash Checks 4 Less is now claiming they are the HDC and claiming that Guy's Grocery Store owes them the funds for the check. Guy's Grocery Store has now reached out to Paying Bank because they don't feel they should have to pay the same check twice.

What's the best course of action?

Holder in Due Course



Remote Deposit Capture Indemnity

- Indemnity to protect second depository bank that received deposit of paper check that was returned unpaid because the check was previously deposited at another depository bank using RDC service
- Indemnity provided by first depository bank that
 - Is truncating bank because it accepts the deposit of electronic image or electronic information related to the original check;
 - Does not receive original check;
 - Receives settlement or other consideration for electronic check or substitute check related to the original check; and
 - Does not receive return of check unpaid

RDC Indemnity

Depository bank indemnifies second depository bank that accepts original check for deposit, for losses incurred by second depository bank if loss is due to check having already been paid

Scope of damages limited to consideration received plus expenses/attorney's fees

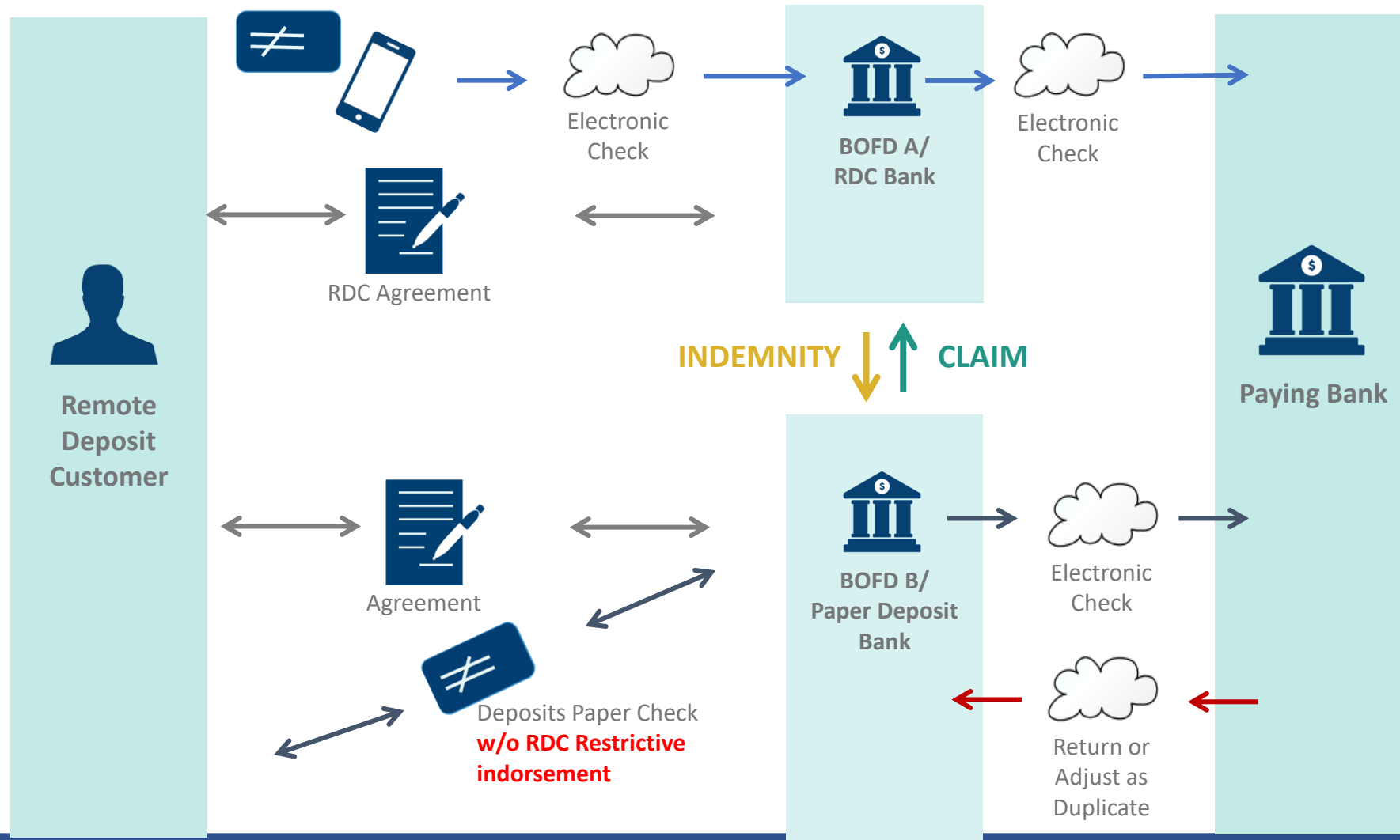
Comparative negligence defense available



Depository bank does not make indemnity if original check bore restrictive indorsement inconsistent with means of deposit

Example: “for mobile deposit at [name of first depository bank] only”

Regulation CC Remote Deposit Capture Indemnity



RDC Indemnity Claim Processing

RDC Indemnity claim may be made against any RDC depositary bank that meets the required conditions for providing the indemnity

- Claim can be made to *any* one RDC bank, even if multiple RDC banks are subject to the conditions of the indemnity



For Fed exchanges, use Warranty/Indemnity Claim (WIC) Associated with Remote Deposit Capture (RDC) Items

- Within 90 calendar days of the PAID adjustment or return letter date (after 90 calendar days deal direct)
- Both PAID items must have been processed by Fed
- Check with Fed to ensure conforming with all requirements



For ECCHO exchanges, use Warranty/Indemnity Claim (WIC) for RDC Indemnity Claims within 1 year according to ECCHO Adjustment Matrix

- Use Sample RDC Indemnity Claim letter to provide necessary information

Remotely Created Check (RCC)

Created by a payee under the authority of the account holder

- Not created by Paying Bank
 - Check not created by Paying Bank and that does not bear a signature applied by person on whose account the check is drawn

Reg CC 229.34 (b): Warranty from Depository Bank (BOFD)

- Bank that transfers/presents remotely created check and receives settlement or other consideration warrants to Transferee Bank, any subsequent Collecting Bank, and Paying Bank that:
 - Person on whose account remotely created check is drawn authorized issuance of the check;
 - In the amount stated on the check and to the payee stated on the check

Claim process for unauthorized RCC

- Not provided in Reg CC – claims are covered by rules and agreements
 - ECCHO Rules (Rule 8 or adjustments)
 - FRB OC3 (adjustments)

Remotely Created Checks

- Just in time payments
- Internet payments

**Federal Reserve Retail Payments Study stated 2.3% of checks written are RCCs

Valid RCC must have existed in paper (physical) form prior to imaging

RCCs are vulnerable to fraud because:

- Do not bear drawer's signature – no readily verifiable indication of authorization
 - Consumer complaints of alleged fraud with RCCs
 - Unauthorized RCCs can create risk and cost

Business-size Check

NAME OF COMPANY
STREET ADDRESS
CITY, STATE

101
00-6789-0000

DATE 12-5-09

PAY TO THE
ORDER OF Payee's Name \$ 123.45

One hundred twenty-three and 45/100 Dollars

Financial Institution Name
Street Address
City, State

Memo _____

Authorized by Drawer

⑆00000101⑆ 6⑆000067894⑆ 12345678⑆

Consumer Check

NAME OF COMPANY
STREET ADDRESS
CITY, STATE

101
00-6789-0000

DATE 12-5-09

PAY TO THE
ORDER OF Payee's Name \$ 123.45

One hundred twenty-three and 45/100 Dollars

Financial Institution Name
Street Address
City, State

Memo _____

Authorized by Drawer

6⑆000067894⑆ 12345678⑆

Identify
RCC –
EPC
value '6'

↑
RCC Identification

↑
RCC Identification

↑
Not Signed by Drawer



TS

Electronically Created Item (ECI)

Definition

- Electronic image that has all attributes of an electronic check or electronic returned check but was created electronically and not derived from a paper check

Purpose: to protect ECI transferee bank(s) from certain losses which might include:

- Receiving an unauthorized item
- Receiving a duplicate item

ECI indemnity provided by any bank that transfers ECI to another bank

- Applies to BOFD, collecting and presenting banks

Electronically Created Item Indemnity

Indemnity overview

- Each bank that transfers an ECI indemnifies each transferee bank from losses arising from fact that:
 - Electronic image/electronic information not derived from paper check;
 - Person on whose account ECI is drawn did not authorize item in amount stated or to the payee stated
 - Person that receives or is otherwise charged for electronically-created item is not asked to make payment on an item or check it has already paid (*no duplicates*)

Scope of ECI Indemnity

Applies only
to ECIs

- Not a check, electronic check, electronic returned check or IRD

No specific return reason

- May return as ineligible item

Expeditious return of ECI
not required

- Not considered a check under Reg CC

No adjustments
process in Reg CC

- ECCHO process: Warranty Indemnity Claim (WIC) for Electronically Created Item (ECI) Indemnity Claim
- Fed process: WIC/Associated with Unauthorized Electronically Created Items (UECIs)

Examples of ECIs

- From Reg CC Commentary:
 - Corporate customer electronically creates an image that looks like an image of corporate customer's paper checks and emails the image to the payee
 - Consumer uses a smart-phone application to electronically create and send check image to payee
 - Consumer provides his/her account information to utility which then uses information to create and deposit ECI with its bank to obtain consumer payment

Damage Due to Under-encoding

Linus wrote a check to Sally for \$500. When the check was encoded at Sally's bank, it was only encoded as \$50. Linus failed to notice the incorrect amount processing on his account because he never logs into his online banking. Two weeks later, Sally calls her bank to report that she was only credited for \$50 instead of \$500.

What should Sally's bank do?



FRB Adjustment: Encoding Error (ENC)

- Item was clearly encoded for amount different than legal (written) amount or differs from the stated cash letter/return letter amount
- Timing: Within 6 calendar months of cash letter/return letter date for same day entry
- ECCHO: Amount Error – 180 calendar days

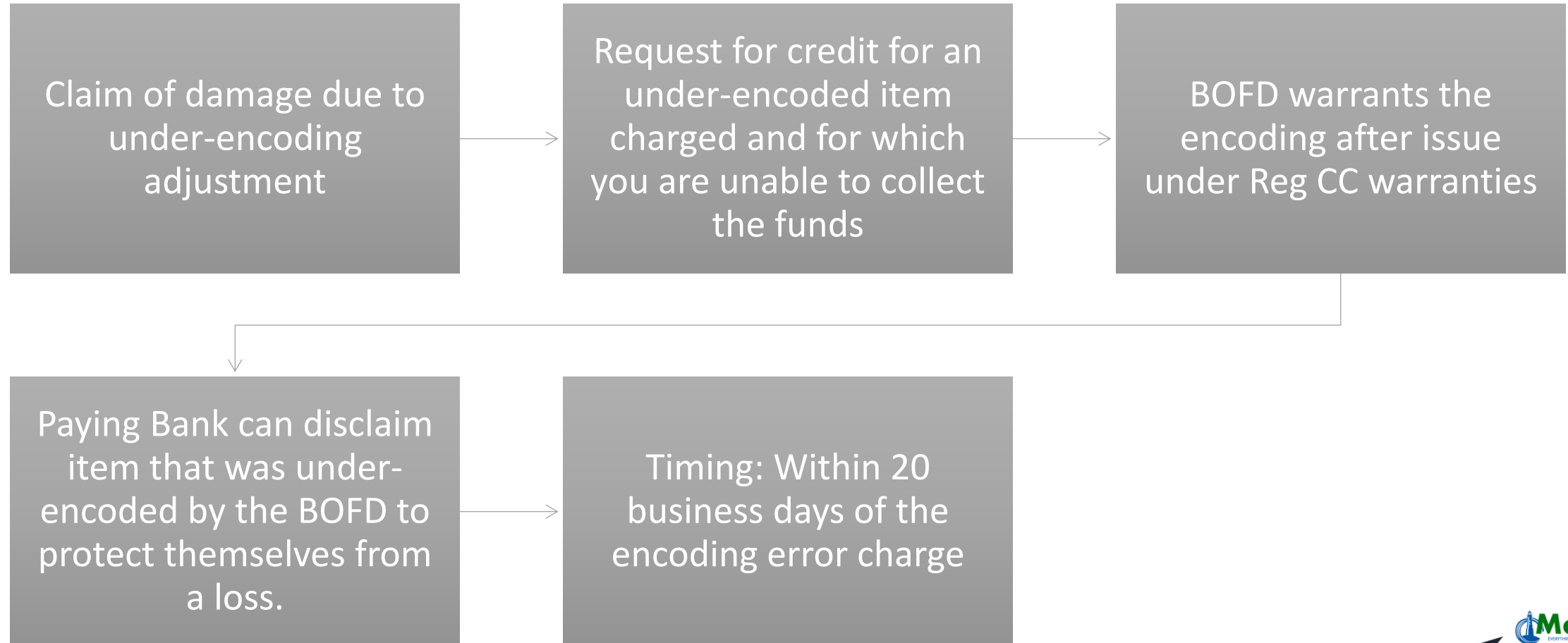
However...

When the Encoding Error Adjustment was received by Linus's Financial Institution, the balance in his account was only \$39.74. Because he wasn't checking his account balance, Linus continued to spend his available funds. Linus's account does not have the money for the \$450 adjustment.

What can Linus's FI do?



FRB Adjustment: Entry in Error (ERR)



Stop Payments

Charlie wrote a check to ComMedia for his cable bill. ComMedia claims to never have received the check. Charlie calls his FI and puts a stop payment on the check, and makes a payment instead with his debit card. In the meantime, ComMedia finds the check, and converts it to an ARC entry.

What can Charlie's FI do?



A few things...

R38 – Stop Payment on a Source Document

- 60 day return time frame
- *What if we are outside the 60 day return time frame?
- *What if the check processed as a check instead of an ARC?
- *What if both the check AND the ARC entry posted to the account?
- *Can we do anything about the debit card payment?

