



Regulation CC and Fraud

Summary

Regulation CC actually implements two separate laws: The Expedited Funds Availability Act (EFAA) and the Check Clearing for the 21st Century Act (Check 21). What it does is it sets forth the requirements that financial institutions make funds deposited into transaction accounts available according to a specified schedule and that they disclose this funds availability policy to its customers. Check 21 is a section of the regulation that breaks down the requirements that affect financial institutions that create or receive substitute checks, including what the requirements are for consumer disclosures and expedited re-credit procedures.

In relation to checks specifically, Regulation CC works very closely with the Uniform Commercial Code (UCC). A collaborated effort by the Uniform Law Commission and the American Law Institute, the UCC was created to simply, clarify and modernize the law governing commercial transactions. It was attempting to make uniform the law among all the states. It facilitated the conduct of various transactions such as purchases, sales, check processing and securing obligations. The UCC has been enacted in all 50 states, District of Columbia, Guam, Puerto Rico and the Virgin Islands, but it does not become law unless it is enacted by legislature and does not have to be adopted exactly as promulgated by the ULC. Louisiana, for example, has not adopted Article 2 (Sales) or Article 2A (Leases) in favor of their civil code traditions governing those transactions. Some jurisdictions adopt non-uniform amendments or fail to enact the latest amendments or revisions. As such, it is important to know what each state's status is in the adoption and implementation of the UCC for each state as there may be discrepancy. For purposes of this manual, it will be referencing the general UCC.

UCC Article 3 and Article 4

The UCC is really the starting point for financial institutions when attempting to determine rights, responsibilities and liabilities relating to issues which checks.

Article 3 and 4 come into play with Regulation CC. Article 3 of the Uniform Commercial Code addresses negotiable instruments, namely drafts, and notes. This includes rules governing negotiability, enforcement, acceptance, tender, transfer, loss and enforceability of certificates of deposit, personal checks, traveler's checks, cashier's checks, money orders and promissory notes, as well as contractual liabilities and obligations of the parties involved.

Article 4 of the UCC covers bank deposits and collections. This includes rules for check deposits, processing, clearing, payment, dishonor, returns, fraud, stop payments, post-dated and stale checks, as well as related deadlines for banks and clearinghouses.

Key Definitions

Checks are negotiable instruments involve three key parties: the person writing the check (the drawer), the person to whom the check is written (the payee), and the bank that holds the checking account (the drawee or payor bank). The person holding, or currently in possession of the instrument, whether or not they are specifically identified on the instrument as the payee, is known generally as the "holder" of the instrument.

Persons entitled to enforce are either the holders of the instrument, a non-holder of the instrument who is in possession and has the rights of a holder, or a person who is not in possession of the instrument who is entitled to endorse the check through some other UCC provisions.

Drawers use checks because it is an easy way for them to pay for goods, services, or other obligations. Payees have an expectation that the check is going to be exchanged for cash at a teller window or credited to their bank accounts upon presentment. And both parties know there are procedures for the collection process and governing laws that offer protections.

Now let us touch on the bank's role in all of this. We mentioned earlier that the payor bank (or drawee bank) is the bank upon which a check is written. The depository bank is the one the payee deposits the check into. The following two terms are used to describe the various banks that handle a check after it is written: collecting bank and intermediary bank.

A collecting bank includes the depository bank, while an intermediary bank is any and all of the collecting banks except for the payor and depository banks. It is important to remember that banks can take on more than one role:

John Adams in Baintree, MA writes a check and mails it to George Washington in Westmoreland County, VA in payment for merchandise. George deposits it in his account at Bank of WCVA in payment for the merchandise. Bank of WCVA is a depository bank and the collecting bank.

Any other bank through which a check travels (except the two banks mentioned above) would be an intermediary bank.

Elements of a Negotiable Instrument

Like mentioned above, negotiable instruments are governed by the legal requirements of UCC Article 3. In order to satisfy the requirements of negotiability, checks must be the following:

- Written and signed
- Payable to bearer or to order
- For a fixed amount of money
- An unconditional order or promise to pay
- Payable on demand or at a definite time.

Let us break down some of these requirements:

1. Written and Signed

Negotiable instruments, like checks, must be in writing and signed by the drawer. Some are signed by a signature machine or stamped with the drawer's signature. That is considered valid as it constitutes an "identifying mark." It is important to remember that some banks have specific procedures for these types of signatures when it comes to identifying marks on a check.

2. Payable to Bearer or to Order

Negotiable instruments are payable to the bearer or to order if the word "bearer" or "cash" is used or if the instrument otherwise indicates that the person in possession of the instrument is entitled to payment. Checks can be payable to an identifiable individual (e.g.- Pay to the Order of John Smith). Once it is endorsed by John Smith (e.g.- on the back of the check, John Smith endorses/signs his name), it becomes a bearer instrument. What that

means is that any person who is in possession of that instrument payable to bearer is the holder of the instrument and can present for payment.

3. Fixed Amount of Money

Negotiable instruments must be for a fixed amount of money. This amount, which can be us U.S. dollars or foreign currency, must be specified clearly and in monetary terms on the face, or front, of the instrument. It cannot be stated in terms of something of value that could be converted to money (i.e.- \$500 US dollars + TV worth \$500 USD is not acceptable). Sometimes, the written amount does not coincide with the numeric amount on the check—if that occurs, UCC Article 3 states that the words control numerals unless the words are ambiguous, in which case the numerals control.

4. Unconditional Order or Promise to Pay

Negotiable instruments are unconditional orders or promises to pay—what that means is that a check is a written order to the bank to pay a specified amount dictated on the check to the payee. This order cannot be dependent on any other conditions—making it unconditional. An example would be a check cannot state: “If he paints my house, pay to order to George Washington.” That is a condition—painting of the house—for the instrument to be ordered and paid. Any instrument that carries this type of condition is not a negotiable instrument.

5. Payable on Demand or at a Definite Time

The date on the check is important—it determines when it is payable. Checks can be postdated (dated in the future) or antedated (dated prior to when the check was written) but it oftentimes causes more of a headache for financial institutions. When you are presented a check that is not dated (either intentionally or unintentionally), the date on that check is considered to be the date it is presented for payment—making it “payable on demand.”

Collection Process

When a depository bank is also the payor bank, then this is known as an “on-us” item and UCC 4-215(e)(2) states that if the check is not dishonored, it is available by the payee “at the opening of the bank’s second banking day following receipt of the item.”

But when the collection is between two different banks, if the collecting banks act before the midnight deadline following receipt, they have acted “seasonably” per UCC 4-202. When the payor bank gets the check, it must pay it, unless the check was dishonored or returned.

Signature and Endorsement

Under Section 3-401 of the UCC, a signature can be made manually or by means of a device or machine, and by the use of any name, including any trade or assumed name, or by any word, mark or symbol executed or adopted by a person with the present intention to authenticate a writing.

Signature is separate from an endorsement. An endorsement is the evidence that the endorser intended the instrument to move along in the channels of commerce. So, it is a signature other than that of the maker, drawer, or acceptor with a purpose of negotiating that instrument or restricting the payment of the instrument (or even incurring the endorser’s liability on the instrument).

A blank endorsement is solely the endorser’s signature alone—it converts the instrument into essentially “like cash.” This type of endorsement does not specify to whom the instrument is to be paid, so it is treated like bearer paper. This assumes, of course, that the first endorser is the person whom the instrument was payable to originally. For example,

if a check was endorsed by the payee John Smith (signed on the back), it can be passed from one person to another and cashed in by any of them. Blank endorsements can be negotiated by delivery alone unless a holder converts it into a special endorsement.

A special endorsement names the transferee-holder. The payee of the check can endorse it over to a third party in writing “Pay to the order of [name of third party] and then sign his name. Once a check is specially endorsed, the check can only be negotiated further when the special endorsee adds his own signature.

A restrictive endorsement attempts to actually limit payment to a particular person or prohibit further transfer or negotiation of the check. Two legitimate restrictive endorsements are permissible—collection endorsements (i.e.—“For Deposit”) or trust endorsements (i.e.- “Pay to John Smith in trust for Thomas Jefferson”).

Alterations and Counterfeit

Alterations

Alterations are specifically mentioned in UCC 3-407 and are defined as unauthorized changes in an instrument that purports to modify in any respect to the obligation of the party. It can also be the unauthorized addition of words or numbers or other changes to an incomplete instrument relating to the obligation of a party.

Material versus immaterial alterations are important to note. A material alteration is one that modifies in any respect the obligations of a party. Examples include:

- Changing the number or relations of the parties
- Changing the payee name
- Backdating the date of a postdated check
- Any increase or reduction in amount
- Completing an incomplete check other than as authorized
- Deleting restrictive “Only for Deposit” endorsements; and
- Any other unauthorized addition or deletion which would change the contract of the parties.

Immaterial alterations do not change the obligations of the party. Examples include:

- Inserting, deleting or changing any memorandum on the check that is not part of the “contract” or obligation
- Changing an impossible date (i.e.- September 31st) to the next possible date
- Conforming the check figures to the written amount
- Non-fraudulent reduction of amount to reflect a part payment
- Addition of a date to the check; and
- Addition of words on the payee line that do not change the payee.

Liability for losses as a result of alterations are mixed—sometimes the drawer of the check bears the loss and other times the drawee and depository bank bear the loss. Although a maker’s bank is liable to the customer for paying an altered item, the depository bank (or depositor if available) usually ends up be responsible for the loss. Unless the maker was negligent, ratified the transaction or is precluded from asserting a claim, they will not be liable for an

unauthorized material alteration of the check. The payor bank can charge its account for the check only as it was originally drawn (assuming the bank acted in good faith).

The depository and the collecting banks warrant to the payor bank that the item has not been altered. That makes them liable to the payor bank for damages for breach of warranty equal to the amount paid by the payor bank, minus the amount the payor bank is entitled to receive from the drawer because of the payment, plus any compensation for expenses and loss of interest resulting from the breach. Rights of the payor bank to recover damages are not going to be affected by any failure on its part to exercise ordinary care in making the payment.

Depositors who deposit an altered item are liable to the depository bank for damages that arise from the alterations.

Defenses

The first defense is that the alteration was not a material alteration. Many changes to an instrument are not going to account as an alteration. If an alteration does not change the obligation of any party, it is not covered. Section 3-114 discusses contradictory terms of instruments and it provides that if an instrument contains contradictory terms, type-written terms prevail over printed terms and handwritten terms prevail over both, and words prevail over numbers. So, if an instrument had contained contradictory terms and it was changed so that the number agreed with the words, that would not be a material alteration because the general obligation of the parties did not change. Another common example is the date—the date being listed as February 30th is impossible so a check can be altered to reflect the correct date but that is not legally considered an alteration.

A second defense is a change was authorized—Section 3-407 requires an alteration to be unauthorized changes or additions of words or numbers—but if you can prove that it was an authorized change, there is no alteration.

Third is customer negligence. The customer was careless with their checks, they didn't hire a trustworthy bookkeeper, they failed to take preventative actions after learning about a forgery or alteration, or they negligently made a check out leaving large spaces for someone to fill in some extra zeros.

Next is unauthorized completion—if there is an incomplete instrument that is altered by some unauthorized completion, the payor bank paying it or the person taking it for value, if they did so in good faith and without notice of the alteration, can enforce rights on that instrument according to its terms as completed.

Original terms are important—if an instrument was fraudulently altered, it can still be enforced according to its original terms by the one who has paid it or taken it in good faith for presentment and without notice of the alteration. So, if a check was written originally for \$100 and was altered to read \$1,100, it could still be enforced for \$100.

Next is negligence—if some other party like the drawer or the payee or the drawee or depository bank were negligent in a way that substantially contributed to the loss from the alteration, they are precluded, or stopped, from asserting the alteration claim against a person who, in good faith, relied on and paid that instrument or took it for value. There is a comparative fault rule here. It proportionally assigns fault between the responsible parties.

Customers have requirements as well. A customer's failure to examine and report is important. If the drawer of the check failed to promptly examine their bank statement and report any alterations within a reasonable time (so 30 days), the drawer cannot pass the loss on to his bank. His bank is then precluded or stopped from passing it on to the depository bank unless the drawer can show that his bank failed to exercise ordinary care. If that were the case, the loss is going to be split up and allocated between the parties to the extent that the failure of each to exercise ordinary care contributed to the loss.

Then, there is a one-year bank statute of limitations. Besides a drawee bank's ordinary care of lack of, if a customer fails to report the alteration within 1 year of receiving the item or the statement, the customer is barred from passing on the loss.

Lastly, there are the issue of repeat offenders—these are repeat wrongdoers where, if the alteration is the work of someone who is a repeat wrongdoer, then the customer is stopped from passing along the loss.

Counterfeit

A counterfeit check is not defined in the UCC specifically, but it is essentially a check that is presented based on false identification or false checks drawn on valid accounts.

UCC Warranties

Warranties are what provide protections and recourse when there has been a breach of either a transfer, presentment or encoding warranty.

Transfer Warranties

Transfer warranty refers to an implied promise regarding the title and credibility of an instrument made by a transferor to a transferee. Generally, transfer warranties are made for transfers through endorsements. A transfer warranty can also be granted to any remote transferee through endorsement on the instrument. If a transfer has been made without an endorsement, then only an immediate transferee is granted transfer warranty by a transferor.

There are six warranties prescribed within a transfer warranty:

- No forged or missing endorsements;
- All signatures are authentic and authorized;
- Item has not been altered;
- Item is not subject to a defense or claim in recoupment;
- Warrantor has no knowledge of insolvency proceeding on maker, acceptor or drawer; and
- For remotely-created items, person on whose account it is drawn authorized its issuance and in the amount drawn.

Presentment Warranties

When dealing with negotiable instruments, a presentment warranty refers to an implied promise for the title and credibility of an instrument made by a payor or acceptor upon the presentment of the instrument for payment. Under UCC 3-417(a), if an unaccepted draft is presented to the drawee for payment or acceptance and the drawee pays or accepts the draft, the person obtaining the payment or acceptance, at the time of presentment, and the previous transferor of the draft, at the time of transfer, warrant to the drawee making payment or accepting the draft that in good faith:

- The warrantor is, or was, at the time the warrantor transferred the draft, a person 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;
- The draft has not been altered;
- The warrantor has no knowledge that the signature of the drawer of the draft is unauthorized; and

- With respect to any remotely created consumer item, that the person on whose account the item is drawn authorized the issuance of the item in the amount for which the item is drawn.

UCC Golden Rule 4-401

A bank cannot pay a check drawn on a customer's account unless the item is properly payable.

Encoding Warranties

The encoding warranty covers a person who encodes. Most often, this will be the depository bank but it can also include bank customers, especially those who process large volumes of checks and who do their own encoding. When this occurs, both the customer who did the actual encoding and the depository bank make the warranty. The warranty is made to any subsequent collecting bank and to the payor bank or other payor. Banks included in the forward collection process, payor banks, and non-bank payors, like insurance companies issuing payable through drafts, benefit from this warranty. It provides that any information encoded on the check by the person making the warranty has been correctly encoded. It covers the amount field and all entries made by the warrantor on the MICR line as well.

Midnight Deadline Rule

Under UCC 4-302(a), a payor bank must pay or return an item or send notice of dishonor by midnight on the next banking day following the banking day on which the bank receives the item. If a bank fails to do so, it is liable for the amount of the item. Payor banks must return a check within their midnight deadline. The bank returns a check for purposes of the midnight deadline when the check physically leaves the bank's remises to be delivered to the collecting or depository bank.

Payor banks essentially have three duties when returning forged, altered, or unauthorized checks. They must return the check by the midnight deadline in accordance with the UCC. They must expeditiously return the item. And they must send notice of nonpayment for checks in accordance with Regulation CC.

The collecting bank must be exercising ordinary care. They need to exercise it in presenting an item for collection, in sending notice of dishonor or nonpayment or returning an item, and in settling for an item when the bank receives final settlement. They also must notify the transferor of any loss or delay.

If the depository bank provided provisional credit to its customer for a deposited item that is later dishonored for any reason, it can revoke the settlement given by it, charge back the amount of any credit given to its customer for the item, or it can obtain a refund from its customer if, by its midnight deadline or within a longer period after it learns the facts, it returns the item or sends notification of the facts to the depositor. If returns or notice is delayed beyond the depository bank's midnight deadline, it can still revoke the settlement, charge back the credit or obtain a refund, but now it is liable for any loss resulting from the delay.

Always note, a bank cannot return a check after it has been finally paid. Final payment occurs when the bank does any of the following:

- Pays the item in cash;
- Settles for the item without having a right to revoke the settlement under statute, clearing house rule or agreement;
- Makes a provisional settlement for the item and fails to revoke the settlement in the time and manner permitted by statute, clearing house rule or agreement.

Finally paid means the bank becomes accountable to the presenter for the amount of the item unless it has a valid defense.

Types of Fraud

Forged Maker Endorsement

A forged maker instrument is any item bearing an unauthorized payor signature. The person who signs the check, making them responsible for the payment, is known as the maker of the check. So, a forged maker scheme is really just a check tampering scheme in which an individual steals a check from an unsuspecting, legitimate customer of a financial institution and then forges the signature of an authorized maker on the stolen check. Forgers then can make the checks payable to themselves or others and have the cashed or deposited.

Customers are not liable for a check drawn on their account that they did not sign or benefit from its proceeds. Because, without a customer's signature, the check is not considered properly payable ("Golden Rule"). When looking at liability on forged maker checks, between the maker's bank and the depository bank (or any collecting bank), the maker's bank is usually liable for a forged maker signature.

*A counterfeit check is generally treated as a forged maker check.

Payor Bank Defenses

There are defenses to forged maker claims for the payor bank. The payor bank may be able to shift the loss from the unauthorized signatures by agreement with its customer in certain limited cases (e.g.—facsimile signature or cash management agreement).

Additionally, banks are not liable for paying a forged check if its customer had approved the transaction, ratified the forgery, or otherwise was precluded from making a claim (e.g.—customer intentionally fails to report the forgery, requests the bank not to prosecute, or enters into a direct settlement with the forger).

There is also the "repeat wrongdoer rule" whereby a customer has a duty to promptly examine account statements and returned checks, and to notify the bank of any unauthorized signatures. That customer would be liable for unauthorized signatures or alterations by the same wrongdoer if the customer failed to discover or report the problem to the bank within a reasonable time (which is not to exceed 30 days or any shorter prior set forth in the customer's deposit agreement) following the mailing of the first statement or check reflecting the forgery or alteration.

But it is not quite that simple with the repeat wrongdoer rule. The bank cannot have failed to exercise ordinary care. If the customer could prove that the bank failed to exercise ordinary care in paying the item and that the failure contributed to the loss, then that loss is going to be allocated between the customer and the bank to the extent that each contributed to the loss. If the bank is proven to have lacked good faith, then the customer is not stopped from asserting the forgeries because of his failure to act in a timely manner.

Lastly, without regard to lack of care by either the customer or the bank, if a customer does not discover and report forgeries or alterations within 1-year after the statement or items were made available to him, that customer is precluded from asserting the unauthorized signatures and alterations.

Depository Bank Defenses

Depository banks are generally not liable for forged maker checks if they act with ordinary care. If the depository bank acts with ordinary care, the payor bank is going to be liable for the check if it fails to return it within its midnight deadline.

Forged Payee Endorsement



Forged payee endorsements also generally involve stolen checks—it is an item bearing an unauthorized payee signature. Forged endorsements occur when a validity drawn check is fraudulently endorsed. Forged endorsed items are being cashed by individuals claiming to be the true payee or are second endorsed and presented by the second endorser as valid. Remember that a forged endorsement is different than a forged signature on a check. Forged endorsements involve forging the payee's signature for negotiations. Generally, forged endorsed checks are going to contain the true signature of the account holder.

Depository and collecting banks are the ones warranting that there is good title and that no endorsement necessary to title has been forged. A payor bank is going to be liable for forged payee checks. Between the depository bank and the payor bank, the depository bank is usually liable for forged payee checks. And when it is between the depository bank and its customer, the customer is liable for forged payee checks.

Liability is going to be limited to the loss suffered by the breach, but not more than the amount of the check plus expenses and the loss of interest incurred as a result of the breach. Because forged payee endorsements are ineffective, depository and collecting banks are going to be held liable to subsequent transferees (e.g.—the payor bank) and can recover from previous transferors for breach of warranty based on forged endorsements. However, the payor bank has a right to recover its loss from the collecting bank for breach of the presentment warranties.

It is important to note that persons who take checks with forged or missing endorsements are not holders and cannot be holders in due course (see Holder in Due Course section below), even if they act in good faith and take the checks for value and without notice of a defense or claim.

Depository Bank Defenses

There is always a claim that no forgery took place—the check was deposited without a signature, or with a different name in the space for the payee's endorsement. There are some situations where a payor bank is not liable to its customer, meaning depository and collecting banks would also not be liable for forged payee checks. This can occur with the payor bank's customer is precluded from asserting a claim by its failure to exercise ordinary care or to review their statements and report forgeries in a timely manner. If the payor bank asserts a claim for breach of warranty based on an unauthorized signature or alteration, the depository bank can defend by proving that:

- The endorsement is effective under the imposter rule, the fictitious payee rule or the responsible employee rule; or
- The payor's customer is precluded from asserting the unauthorized endorsement or alteration against the payor due to the customer's lack of ordinary care or its failure to report the problem in a timely manner.

There are cases where the maker or intended payee were negligent—if the bank acts in good faith and in accordance with reasonable commercial standards, the maker or intended payee can be precluded from asserting the unauthorized signature. But, if the bank contributed to the loss by its failure to exercise ordinary care, that loss can still be allocated between the parties to the extent each contributed to the loss.

Always remember that the depository and collecting banks are discharged to the extent of any loss if the party asserting the warranty claim did so after an unreasonable delay—claims against the depository or collecting bank for breach of warranty have to be given within 30 days after the claimant had reason to know of the breach and the identity of the warrantor.

Holder in Due Course

A holder in due course (HIDC) is from the UCC and is more than just anyone who accepts a check for payment. A HIDC receives the benefit of getting an instrument free of claims or defenses by previous possessors. They have a preferred position in line and can treat the instrument almost as if it were money. But there are some caveats to this.

The transferee must still be the following:

- A holder of a negotiable instrument
- Have taken it:
 - For value
 - In good faith
 - Without notice:
 - That it is overdue or
 - Has been dishonored (not paid) or
 - Is subject to a valid claim or defense by any party or
 - That there is an uncured default with respect to payment of another instrument issued as part of the same series or
 - That it contains an unauthorized signature or has been altered, and
- Have no reason to question its authenticity on account of apparent evidence of forgery, alteration, irregularity, or incompleteness.

So, what that means is that on the face of the check, there cannot be any evidence of fraud. The person accepting the check cannot have knowledge of any underlying fraud related to that check. As such, under the UC, the recipient of a check is a HIDC and it entitled to be paid for the check. That is true even if the drawer of the check placed a stop payment on the check, or the check was rejected at the bank as a positive pay exception item. If the recipient (our HIDC) is unable to negotiate the check (i.e.- get paid), the HIDC can sue the drawer for the full-face value of the check and can receive judgment against the drawer.

There is a statute of limitations on how long after a HIDC can sue the drawer—it has been set to 10 years from the issue date or 3 years from the date the check was deposited and returned unpaid, whichever comes first.

Late Returns and Defenses

A bank can return a check after its midnight deadline if it acts to return the item to the depository bank (or to a returning bank) in a highly expeditious manner (i.e.- courier) so that it is received by the close of that bank's banking day following the expiration of the midnight deadline.

If a bank received a check for payment before its cutoff on Monday, it can return the check by courier to the depository bank by the close of the banking day on Wednesday, even though the normal midnight deadline would have been passed at midnight on Tuesday.

Not all late return claims are a loss. One of the most common defenses is when a check has been paid over the payee's forged or missing endorsement. When this happens, UCC places the ultimate liability for the loss on the depository bank. The depository bank is the one who warrants to the payor bank at the time it transfers a check for payment that it has good title to the item, and that it has been vetted.

Generally, forged to missing endorsement claims happen long after the forged check was presented to the payor bank for payment. When this happens, the depository bank can either attempt to avoid liability on a breach of warranty claim by asserting that the forged check was returned for refund after the payor bank's midnight deadline expired, which would make the payor bank accountable for the item.

Payor banks are not subject under UCC to the depository bank's late return claim when the check being contested contains a missing or forged endorsement. UCC states that the liability of the payor bank to pay an item that has been returned after the midnight deadline has expired is still subject to defenses based upon a breach of warranty of good title or proof that the person seeking enforcement of the late return liability presented or transferred the item for the purpose of defrauding the bank. A payor bank's liability for a late return is moot if the check in question bears a forged or missing endorsement.

Other common defenses include emergency conditions, consent to hold, the bank actually did meet the midnight deadline, mistake, or the check was sent for collection.

Regulation CC and Fraud FAQs

Scenario 1: A business account's checkbook was stolen, and fraudulent checks have been written. How many days does the bank have to return fraudulent check (non-remotely created)?

Scenario 2: The bank recently deposited a check that was made payable to multiple parties into the account of one of the named parties. One of the other named parties is now contacting the bank because they did not receive any funds from the check. Upon review, the noticed that this check was not endorsed by any of the named payees. What if anything are we required to provide to the second payee who is asserting they received no benefit from the check?

Scenario 3: The bank had a teller cash an On-Us check for a non-customer. The check had a written date of 2019 and the check also had printed "Void after 90 days." Is the bank allowed to charge a customer's account for a stale-dated check?

Scenario 4: How long can a person make a claim on a check regarding an endorsement? For example, a check is made payable to John and Jane Doe. John signs the check and deposits it into his sole account. Jane gets word and wants to make an endorsement claim. What is that time period?

Scenario 5: Can an official check/cashier's check can be returned as a forgery item?

Regulation CC and Fraud Answers

Scenario 1: Typically it is going to be the midnight deadline in that case: (10) "Midnight deadline" with respect to a bank is midnight on its next banking day following the banking day on which it receives the relevant item or notice or from which the time for taking action commences to run, whichever is later." Model UCC § 4-104(a)(10).

Generally, the payor bank is going to be liable for checks that are not returned by the midnight deadline (i.e.—the midnight of the banking day after the date of presentment) for a forged maker's signature. If the bank did miss the midnight deadline, it would potentially make a claim using one of the UCC defenses.

Scenario 2: Here it depends on how it was written: "and" or "or." Meaning, did it require all signatures or not? Assuming here it was written as "and" and requiring all signatures, then it becomes a UCC claim. The payee or maker of the check can file a UCC claim for improper endorsement. The payee can only do so if they were in possession of the check. If they never received payment, then they would need to make a claim against the person who owes them money—i.e.- the other payee or the original maker of the check. If they did contact the maker, the maker could come back with a claim for improper endorsement. With larger checks, it is always best to involve legal counsel as state UCC laws are now involved.

Scenario 3: Under UCC, the bank can charge the account for the check even if it is stale dated. But for UDAAP purposes, the bank may want to inform its customer. Sometimes there is an issue when the drawn-on bank is someone else and they have filed a lost/stolen affidavit. For UCC purposes, a drawn-on bank can return a check if it is older than 6 months. They are not actually obligated to, however.

Scenario 4: It is interesting here that the check was made out to "John AND Jane" and the paying bank did not return the check when John was the only endorsement. Technically, if the "and" instead of the "or" is used, both should sign, or it is not a valid endorsement (although watch out! Some banks oftentimes ignore this rule). As the paying bank in this scenario, they would be liable under UCC for 3 years. Regulation CC holds as well as indemnities may need to be involved in this scenario.

Scenario 5: This can vary slightly based on state law, but, as long as the drawn-on bank returned the item to you by the midnight deadline, they can in fact return a forged item. If they are beyond the midnight deadline, then it falls outside the UCC and whether they can return it would depend on whether you both are members of the ECCHO Agreements: <https://www.eccho.org/uploads/Rules%208%20%209%20White%20Paper.pdf>