

U B A F a l l C o m p l i a n c e C o n f e r e n c e

# Regulation CC and Fraud

Presenter: Elizabeth K. Madlem

# Agenda

- Basic Background
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  - Elements of a Check
  - Technical Terms
- UCC Warranties
  - Types of Warranties
- Fraud and Liabilities
  - Forgeries
  - Check Alterations/Counterfeits
  - Defenses
- COVID-19 and Check Fraud
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## BASIC BACKGROUND

# Regulation CC Scope

- Regulation CC implements the Expedited Funds Availability Act of 1987—sets certain standards for endorsements on checks that are paid by banks and other depository institutions
- Requires financial institutions to provide account holders with disclosures that indicate when deposited funds will be available for withdrawal
- Addresses long hold times, including implementing maximum hold times
- Enactment of the Check Clearing for the 21<sup>st</sup> Century Act allows check collection among banks in the U.S. to become predominantly electronic-based

# Basic Background: Elements of a Check

1 William Garcia  
2063 PLEASANT RD  
ANYWHERE USA 12345

2 April 10, 2013

9 201  
000-00000

3 Pay to the Order of Grocery Store

4 \$ \$46.73

5 Forty-six and seventy-three/100

6 Your Bank Street Address  
City, State 12345

7 For Groceries

8 William Garcia

11 1234000567

10 9876543201

13 ENDORSE CHECK HERE  
for deposit only  
John Doe

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE

1. Maker Information
2. Date
3. Payee
4. Numeric Dollar Amount
5. Written Legal Amount
6. Bank Information
7. Memo Line
8. Make Signature Line
9. Check Number
10. Account Number
11. Routing (ABA) Number
12. Payee endorsement
13. Restrictive endorsement

# Basic Background:

## Breakdown of UCC & Technical Terms

TERM	UCC SECTION	DEFINITION
<b>Negotiable Instrument</b>	UCC 3-104	Either a draft or a note
<b>Bearer or Order To</b>	UCC 3-109	Bearer is the one holding the check; Order to is an identified person
<b>Holder</b>	UCC 1-201	If payable to a Bearer, the person in possession of check; or if to Order To, the identified person in possession
<b>Person Entitled to Enforce</b>	UCC 3-301	Person who is: 1) the holder of the instrument; 2) a non-holder in possession who has rights of a holder; or 3) a person not in possession who is entitled to enforce through UCC provisions
<b>Holder in Due Course</b>	UCC 3-302	Physically has an instrument without forgery, alteration or it being incomplete and expects payment

# Basic Background:

## Technical Terms Continued

TERM	UCC SECTION	DEFINITION
Payor Bank/Drawee	UCC 4-105 / 4-104	The bank ordered to make payment when an instrument is presented
Presenting Bank	UCC 4-105	The bank that presents an instrument to the Payor Bank for payment
Depository/Collecting Bank	UCC 4-105	The bank that accepts the instrument for deposit or payment
Payee		Person to whom the instrument is made payable to
Maker/Drawer	UCC 3-103	The person who promises to pay the instrument amount, generally a customer of Payor Bank
endorser and Types of endorsements	UCC 3-204	A person who signs the check other than the Maker, Drawer or Acceptor (Blank or Restrictive endorsements)



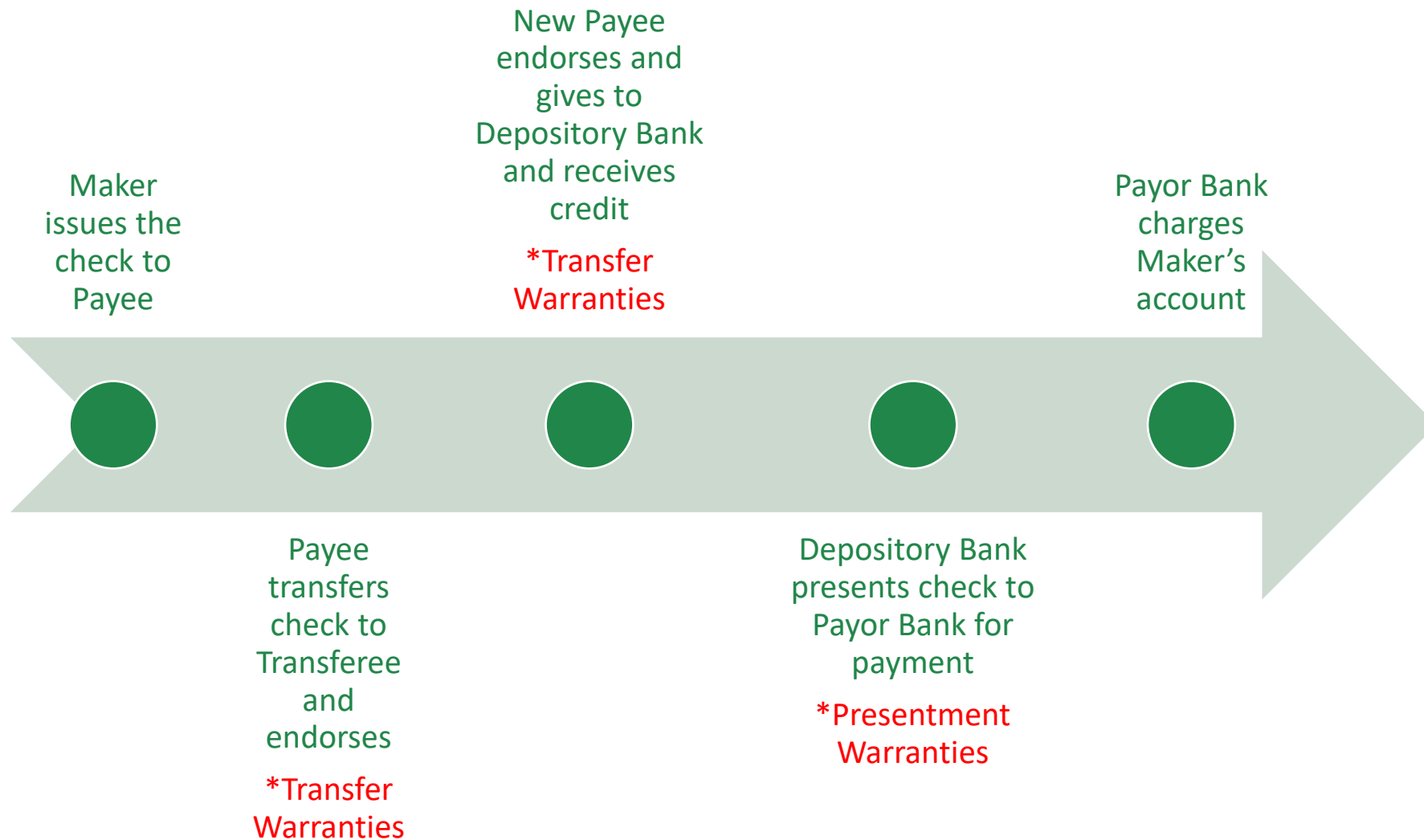
## CHECK FRAUD



# The UCC Warranties

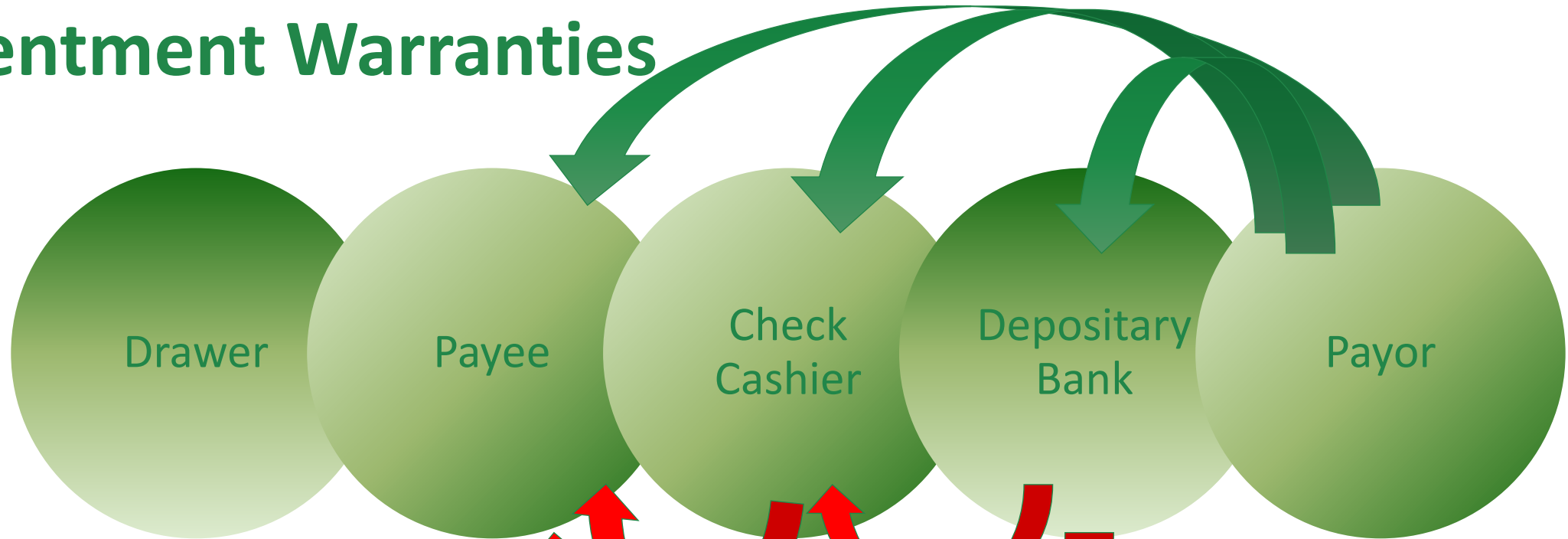
TRANSFER WARRANTY	PRESENTMENT WARRANTY	ENCODING WARRANTIES
UCC 4-207	UCC 4-208	UCC 4-209
6 Separate Warranties:	Payor Bank and person accepting payment warrant:	A person who encodes information on or with respect to an item after issue warrants to any subsequent collecting bank and to the Payor Bank that the information is correctly encoded
1. No forged or missing endorsements	1. Person accepting payment (Warrantor) was entitled to enforce	*If customer of depository bank encodes, that bank also makes the warranty.
2. All signatures are authentic and authorized	2. Draft has not been altered	
3. Item has not been altered	3. Warrantor has no knowledge signature if unauthorized	
4. Item is not subject to defense or claim in recoupment (UCC 3-305(a))	4. For remotely-created consumer item, person on whose account drawn actually authorized issuance for that amount.	
5. Warrantor has no knowledge of insolvency proceeding on maker, acceptor or drawer		
6. For remotely-created item, person on whose account it's drawn authorized its issuance in the amount drawn		

# Life of a Check in Warranties

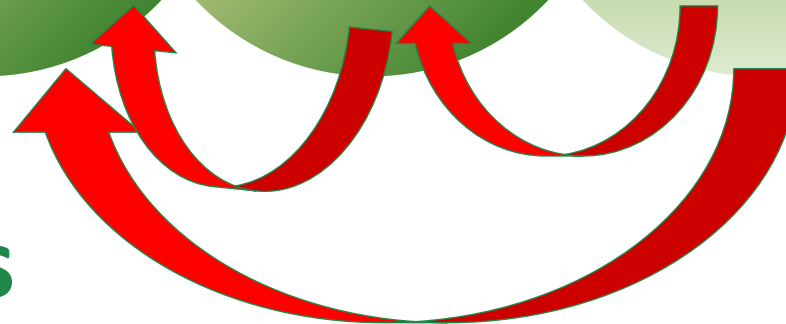


# Warranties

## Presentment Warranties



## Transfer Warranties



# Types of Fraud:

## Forged Payee Endorsement

**\*Generally  
involves stolen  
checks!**

### The Golden Rule UCC 4-401

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

### Signature: UCC 3-401

- Made manually or by a device/machine and by the use of any name, word, mark or symbol with intent to authenticate

### Hypothetical

- Person A, a customer of Bank X, makes a check payable to Person B. Person C steals check, endorses and deposits into Bank Y.

# Types of Fraud: Forged Maker Signature

**\*Generally involves  
stolen blank checks!**

Perpetrators will forge Maker's signature, making check payable to:

- Self
- Accomplice
- "Cash"
- Vendor/Third Party

## Hypothetical

- Person A has his check stolen by Person B. Person B writes the check to herself (Payee is Person B), and then signs/forges Person A's signature. Person B endorses the check to Bank X, who then forwards it to Bank Y for payment.

# Types of Fraud:

## Check Alterations and Counterfeits

TERM	UCC SECTION	DEFINITION
Alteration	UCC 3-407	Unauthorized change in an instrument that attempts to modify in any respect an obligation of a party; OR an unauthorized addition of words or numbers or other change to an incomplete instrument relating to a party's obligation
Counterfeit	--	Presented based on false identification or false checks drawn on valid accounts.

# Forgery Liabilities

## HYPOTHETICAL

1:

- Person A, a customer of Bank Y, makes a check payable to Person B. Person C steals check, endorses and deposits into Bank X.

Breach

- UCC 4-208: Presentment Warranties

## HYPOTHETICAL

2:

- Person A has his check stolen by Person B. Person B writes the check to herself (Payee is Person B), and then signs/forges Person A's signature. Person B endorses the check to Bank X, who then forwards it to Bank Y for payment.

Breach

- UCC 4-401: When Bank May Charge Customer's Account

# Alteration Defenses

DEFENSE	UCC SECTION	EXAMPLE
Not a Material Alteration	See as example UCC 3-114	Changing numerical amount to match written word amount
Change was Authorized	UCC 3-407	Correcting date to correct date (June 31 <sup>st</sup> to July 1 <sup>st</sup> )
Customer Negligence	UCC 3-406	Negligently leaves out facsimile signature device
Unauthorized Completion & Original Terms	UCC 3-407(c)	A check was originally written for \$100 but altered to \$1100 it could be enforced for its original amount of \$100
Negligence	UCC 3-406	Payor Bank failed to give timely periodic statements to Maker.
Customer Failure to Examine and Report <ul style="list-style-type: none"> <li>One Year Bar</li> <li>Repeat Wrongdoer</li> </ul>	UCC 4-406	Customer fails to examine periodic statements and notify in 30 days to prevent subsequent forgeries.
Statute of Limitations	UCC 4-111	Precluded if brought up cause of action three years after occurrence.



# Midnight Deadline Rule



- Midnight Deadline: UCC 4-301—Bank must either pay the check or return it by its midnight deadline
  - Midnight of the banking day following the banking day the check is presented for payment (UCC 4-104(10))
  - If a check was presented for payment on Monday, the Payor Bank could either pay it or return it by midnight Tuesday
- A Depository Bank cannot avoid liability to a Payor Bank when it cashes or accept a check for deposit over a Payee's forged or missing endorsement by claiming a Payor Bank failed to return the item by its Midnight Deadline.
- Normally, Payor Bank will be required to pay the entire amount of the check to the holder whether or not it was properly payable.

# But Wait! ... Late Returns and Defenses



- Normally, Payor Bank will be required to pay the entire amount of the check to the holder whether or not it was properly payable.

MISSED DEADLINES	
Returning directly to Bank	Returning Through Federal Reserve
<ul style="list-style-type: none"><li>• Bank can return if acts in highly expeditious manner (ie- courier)</li></ul> <p>Payor Bank receives a check for payment before its cutoff on Monday, it may return the check by courier to the Depository Bank by close of banking day Wednesday even though normal Midnight Deadline would have been Tuesday.</p>	<ul style="list-style-type: none"><li>• Generally, if returning through Federal Reserve, Payor Bank returns check, Federal Reserve credits Payor Bank's account with the Federal Reserve and debits Depository Bank's Fed Account</li></ul> <p>If past the Midnight Deadline, Depository Bank can challenge a late return per FRB's Operating Circular No. 3 by returning the late return back to Fed Reserve noting Payor Bank missed its Midnight Deadline. When Payor Bank is notified about revocation, it can submit statement to Fed Reserve verifying it met Reg CC and UCC deadlines.</p>

# Late Return Defenses

- Breach of Presentment Warranty
- Fraud
- Emergency Conditions
- Consent to Hold Beyond Deadline
- Bank did Meet Midnight Deadline
- Mistake
- Check Sent for Collections



# COVID-19 and Stimulus Check Fraud

## Who will get money?

- Adult U.S. residents that meet established income limits are eligible to receive money from the government. This includes:
  - Taxpayers—people who filed a federal tax return for 2018 or 2019
  - Retirees—people who get Social Security, Railroad or other retirement benefits
  - Beneficiaries—people who get public benefits like SSDI, disability or veterans' benefits
  - Non-filers—people who do not have to file a federal tax return, including people who made no income or made less than \$12,200 (or \$24,400 for married couples)

# Popular Financial Fraud Tactics

- Phishing—while not a new tactic, they are becoming more and more elaborate in gathering sensitive personal and banking information.
- Check scams—common scams involve receiving an unexpected check or counterfeit checks/wire schemes
- Unauthorized or automatic withdrawals—verify any and all deposit and withdrawal agreements in detail
- Financial advisor or personal banker scams—advise customers on your methods of contacting and what information you do or do not request.

# Avoiding COVID-19 Stimulus Payment Scams

1. Only use <https://www.irs.gov/coronavirus/economic-impact-payments> to submit information to the IRS—never respond to a call, text or email.
2. The IRS will not contact a person by phone, email, text message or social media with information about their stimulus payment, or ask for a SSN, bank account or government benefits debit card account number.
3. No one has to pay to receive stimulus money.
4. The IRS will not tell someone to deposit a stimulus check then send them money back because they paid them more than they actually owed.
5. Educate your community. Join ABA's [#BanksNeverAskThat](#) campaign.
6. Help others by reporting coronavirus scams. Visit the FBI's Internet Crime Complaint Center at [www.ic3.gov](http://www.ic3.gov) to report suspected or confirmed scams. You can also stay up-to-date on the latest scams by visiting the FTC's coronavirus page at [ftc.gov/coronavirus](http://ftc.gov/coronavirus).

# Questions?

Thank you for your participation!

We hope you found today's presentation valuable.

If you have any additional questions, please contact Compliance Alliance.

Phone: (888) 353-3933

E-Mail: [info@compliancealliance.com](mailto:info@compliancealliance.com)

<http://www.compliancealliance.com>