

How to Use This Manual

Bank Check Compliance and Liability Protection is designed to acquaint you with the various laws that affect check processing. These laws have a very complex relationship. In some situations, only one law applies, sometimes several do. Sometimes one law will supersede another, but more often you will need to know how to comply with at least two different laws. The following laws are covered in this manual:

- **Articles 3 and 4 of the Uniform Commercial Code (UCC).** UCC Articles 3 and 4 are essentially the only sources of law for forged and altered checks, overdrafts (UCC 4-401(b), (c)), stale checks (UCC 4-404), stop payment orders (UCC 4-303(a) and 4-403)), and wrongful dishonor (UCC 4-402). UCC Article 4 is very important to the timing of check returns, although in this area you also have to look at a federal regulation, Regulation CC.
- **Regulation CC.** Regulation CC (12 CFR 229) is a federal regulation most of which has been in effect since 1988. It applies to all checks drawn on any U.S. office of any bank, with “bank” broadly defined to include credit unions and savings and loans. Subpart C covers check processing rules, chiefly but not entirely on the check-return process. Subpart D (in effect since October 2004) covers substitute checks. Subpart B (which is not covered in this manual) governs check holds and disclosures; Subpart A contains definitions.
- **Regulation J.** Regulation J (12 CFR 210) only applies to checks that are collected and returned through Federal Reserve channels (which is less than 40 percent of all checks that are written in the U.S.), and it generally reinforces the UCC rather than changing it. Regulation J actually has two different parts. In this manual, when we refer to “Regulation J,” we are referring only to Subpart A, on checks.
- **The Federal Reserve Banks’ Circular 3, Collection of Cash Items and Return of Checks.** This is a circular that has been adopted by all the Reserve Banks. It (like Regulation J) applies only to checks that are collected or returned through Federal Reserve channels. It describes various Reserve Bank services, standards, and requirements.

This manual is divided into five sections: Part 1: Check-Processing Rules; Part 2: Forgery; Section-by-Section Analyses; Reference Material; and Examinations. The courses are contained in Part 1 and Part 2. Each course covers a different aspect of check compliance and liability protection, and the information in each course is broken down into manageable lessons with detailed explanations. Illustrations, tips, examples, and references to glossary terms, citations, and other lessons supplement the learning process.

To measure the understanding of the material, the user can take review quizzes at the end of each lesson. Answers to each question are provided in the Administrator’s Handbook at the back of the manual, with explanations and references to the section in the text where the material is discussed. When the user finishes a set of courses and feels confident of his or her knowledge and understanding of the material, the user can take a comprehensive examination. Examinations for Part 1 and Part 2 are provided in the final section of the manual.

Section-by-section analyses of Regulation CC Subparts C and D, Regulation J, and Circular 3 supplement the various courses by providing a handy reference to each and every provision in those regulations and the circular. The Reference Material section includes tables of UCC, Circular 3, Regulation CC, and Regulation J citations, showing where each listed provision is discussed in any of the materials. This section also has a glossary and a very complete index.

Part 1: Check-Processing Rules

A check can be handled in a variety of ways. A bank of deposit can choose to collect a check by presenting the check directly to the payor bank. Similarly, a payor bank can return a check directly to the bank of deposit. Alternatively, a bank of deposit or payor bank can choose to route a check through one or more collecting banks or returning banks. These collecting or returning banks could be Federal Reserve Banks, or they could be private sector banks that collect or return checks in competition with the Fed.

Thus, whether or not a Reserve Bank handles a check is completely within the discretion of the bank of deposit or other collecting bank (for forward-collection checks), and the payor bank or returning bank (for returned checks).

The UCC and Regulation CC apply to checks no matter how they are collected; Regulation J and Circular 3 apply only to checks that Federal Reserve Banks handle in forward collection or return.

We use a transactional approach to lead you through how the specific laws/regulations—UCC Articles 3 and 4 and Regulation CC (and, when relevant, Regulation J and Circular 3)—affect various aspects of check handling.

Courses

- Course 1: Midnight Deadline for Payor Banks
- Course 2: Expeditious Return—Paying Bank Responsibilities for Returned Checks Under Regulation CC
- Course 3: Notice of Nonpayment
- Course 4: Returning Bank Responsibilities for Returned Checks
- Course 5: Bank of Deposit Responsibilities for Returned Checks and Notices of Nonpayment
- Course 6: Enforcing Midnight Deadline Liability
- Course 7: MICR-Encoding and Other Check-Format Issues
- Course 8: Settlement
- Course 9: Substitute Checks, Electronic Items, and Other Nontraditional Checks

Part 2: Forgery

When a check is forged, someone must bear the loss. The main source of law governing liability for forged checks (checks with forged drawer signatures), checks with forged endorsements, and altered checks is the Uniform Commercial Code (UCC). In Part 2, you will learn in Course 10 about the liability of payor banks and banks of deposit for checks with forged drawer signatures, and in Course 11 about liability for checks with forged endorsements and alterations and for counterfeit checks. Course 10 also includes some hints for avoiding losses through forgeries and other frauds.

Courses

- Course 10: Liability for Checks with Forged Drawer Signatures

Course 11: Forged Endorsement and Altered Checks

Section-by-Section Analyses

Regulation CC

Regulation J

Circular 3

Reference Material

Reference A: Glossary

Reference B: Table of Cases

Reference C: Table of Circular 3 Cites

Reference D: Table of Regulation CC Cites

Reference E: Table of Regulation J Cites

Reference F: Table of UCC Cites

Reference G: Index

Administrator's Handbook

Administrator's Handbook

Examination Record

Student Records

Course Reviews

Examinations

Bank Check Compliance and Liability Protection is designed to provide your financial institution with an effective and efficient tool for training your compliance and check processing staff. Although great care has been taken to be accurate, check law is complicated, and no attempt has been made to be comprehensive. The law is always changing and you should get legal advice specific to your circumstances if you have any questions about your institution's rights and obligations under the law. No book or guide can substitute for the interactive advice of a knowledgeable lawyer.