



# **67 Days & Counting...**

***Is Your Bank Ready for the July Reg CC  
Changes and Restrictive Endorsements?***

***April 23, 2018***

ADAMS AND REESE LLP

®



# Today's Agenda



- Reg CC Amendments
  - Electronic Checks, ECHs
  - Returns & Notices
  - Warranties, Alteration Presumption
  - Remote Deposit Capture Indemnity
  - Restrictive Endorsements
- Rec CC Industry Preparedness Survey Results
- A Technological Solution to Restrictive Endorsements
- Q&A



# Today's Sponsor



- OrboGraph ([www.orbograph.com](http://www.orbograph.com)), a subsidiary of Orbotech, is a premier developer and supplier of intelligent electronic/paper automation solutions in healthcare revenue cycle management (RCM), as well as recognition solutions, payment negotiability and check fraud detection for the U.S. check processing market.

# Today's Presenters



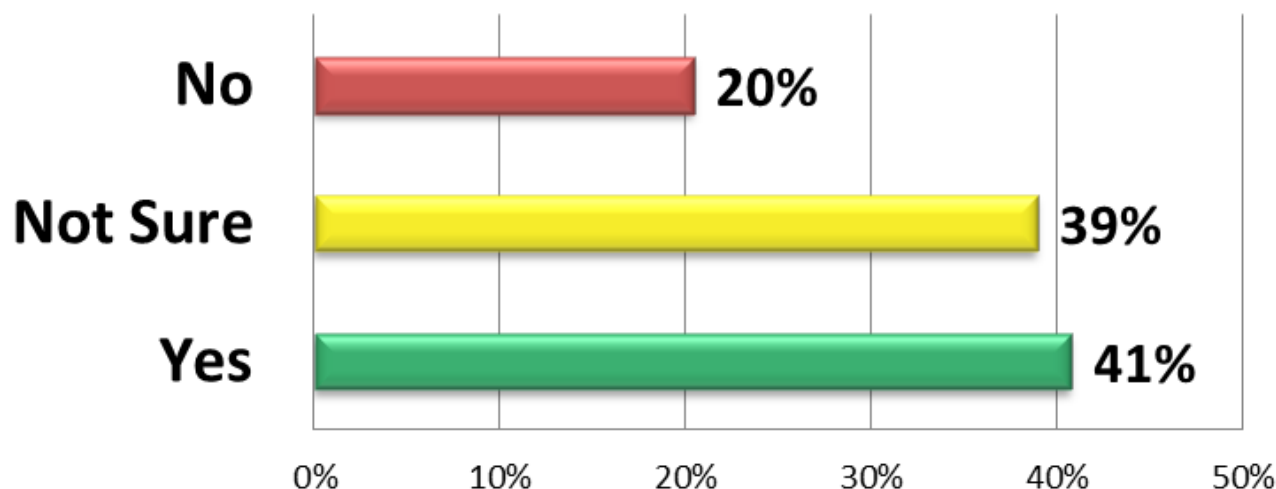
- Paul Carrubba,
  - Adams and Reese LLP
- John Leekley,
  - RemoteDepositCapture.com
- Joe Gregory,
  - OrboGraph



# Industry Preparedness / Action



**Are you making any changes to your Remote Deposit Program related to the upcoming Reg CC changes?**



For more information...:

- [Articles & Resources on RemoteDepositCapture.com](#)
- [FRB Press Release & Link to Reg CC Amendments](#)



# Overview of Reg CC Amendments

## *Effective July 1, 2018*

Paul Carrubba

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ADAMS AND REESE LLP



# Presentation Content



THIS PRESENTATION IS DESIGNED TO PROVIDE ACCURATE AND AUTHORITATIVE INFORMATION REGARDING ITS SUBJECT MATTER.

IT IS PRESENTED WITH THE UNDERSTANDING THAT THE PRESENTER IS NOT RENDERING LEGAL, ACCOUNTING, OR OTHER PROFESSIONAL SERVICES.

IF LEGAL ADVICE OR OTHER EXPERT ASSISTANCE IS REQUIRED, THE SERVICES OF A COMPETENT PROFESSIONAL PERSON SHOULD BE SOUGHT.



# Definitions



- **Electronic Check and Electronic Returned Check**
  - Electronic image of, and electronic information derived from, a paper check or return check that
    1. Is sent pursuant to an Agreement
    2. Conforms to ANS X9.100-87
- **Electronically-created Item (ECI)**
  - Image of a Check
  - Not derived from a paper check





- Checks include Electronic Check or Electronic Returned Check.
- Check does not include an ECI.



# Paying Bank's Responsibility for Return of Check and Notice of Nonpayment



- **Expeditious Return**
  - Received by depository bank no later than 2:00 p.m. local time on second business day
- **Notice of Nonpayment**
  - \$2,500 increased to \$5,000
  - Received no later than 2:00 p.m.
  - Identification of returned check



# Depository Bank's Responsibility for Return and Notice



- Paying Bank liable for expeditious return only if Depository Bank accepts electronic returns
- Acceptance of paper returned checks
- Acceptance of oral notices
  - (1) At the telephone number indicated in the indorsement; and
  - (2) At any other number held out by the bank for receipt of notice of nonpayment.

# Warranties on Electronic Check and Electronic Return



- Presenting and Returning Bank warrants that
  - Image accurately represents information on original and MICR line
- No person will receive duplicate
- Warranty made to any transferee, paying bank and drawer on presentment
- Warranty made to transferee, depository bank and owner

# Warranties on Remotely Created Check



- Person on whose account the check is drawn authorizes check for the amount
- Warranty bank may defend under UCC 4-406

|   |                                       |                       |
|---|---------------------------------------|-----------------------|
| John Smith<br>123 Main Street<br>Anywhere, WI 12345 |                                       | 6370                  |
|   |                                       | Date 02/06/18         |
| Pay to the<br>Order of                              | <b>BEST BUY</b>                       | \$59.00               |
| *****FIFTY-NINE AND 00/100*****                     |                                       |                       |
|   |                                       | 095 - 0955613643- 095 |
| Memo 42693561259698                                 | Authorized by your Depositor 02/06/18 |                       |
| ⑆322232227⑆370283222⑆6370                           |                                       |                       |

# ECI Indemnification

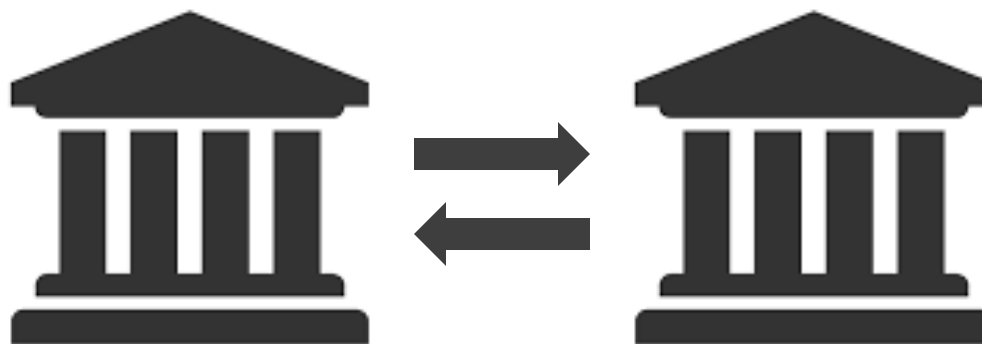


- Transferor indemnifies transferee bank, paying bank and returning bank against loss from:
  - Image not derived from paper
  - Image not authorized or not authorized for amount
  - Duplicate payment
- Notice must be given within 30 days after knowledge

# “Subject to Agreement...”



Presentment and Issuance of checks are subject to agreement between presenting and paying bank.





# Presumption of Alteration



- Presumption of Alteration when the dollar amount or payee have been altered on a substitute or electronic check.
- Presumption may be overcome by evidence or production of the original.

THE FACE OF THIS DOCUMENT HAS A COLORED BACKGROUND ON WHITE PAPER. THE BACK OF THIS DOCUMENT CONTAINS AN ARTIFICIAL WATERMARK - HOLD AT AN ANGLE TO VIEW.

FREIGHT CORPORATION CHACO'S CORPORATION

FREIGHT CORPORATION  
Post Office Box 91 Portland, Oregon 99191

490490

DATE Jan. 15, 2015 CHECK NO. 4906490 NET AMOUNT \$3589.20#

PAY TO THE ORDER OF R. J. Monroe or Maureen Janakowski  
57354 Staci Ln  
Middlebury, IN 46540

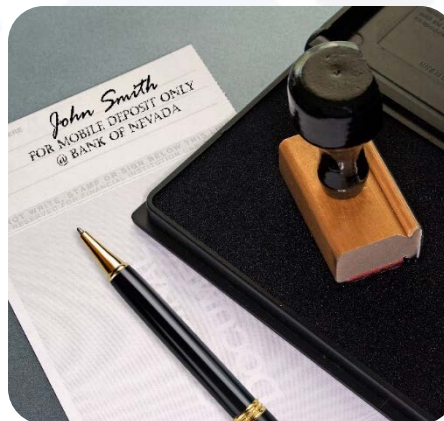
2 SIGNATURES REQUIRED  
Eric Manger  
AUTHORIZED SIGNATURE

⑈490490⑈ ⑆379309379⑆ 336⑈2⑈33679⑈

# Remote Deposit Capture Indemnity by Depository Bank



- Depository Bank that accepts RDC indemnifying Depository Bank that takes an original check
  - From loss caused by duplicate
- No indemnification if check contains Restrictive Endorsement



# RDC Indemnification Example



One Check,  
Multiple  
Deposits



Depository FI's



Bank A

Clearing

Returns

Paying / Bank

If Check has No Restrictive  
Endorsement A Indemnifies B  
and Claim is valid.

If Check has Appropriate  
Restrictive Endorsement For  
Deposit to Only to Bank A,  
Claim is invalid by Bank B.



Bank B

# Indemnity - Discussion



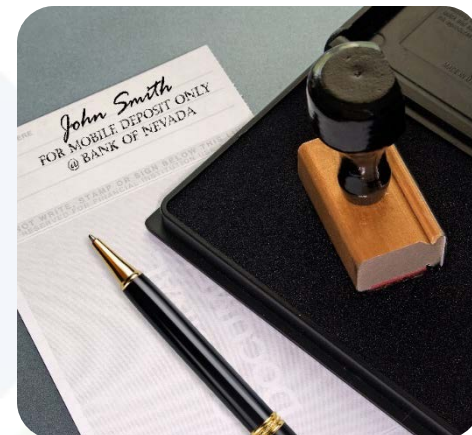
- Scenario #1:
  - Single Mobile Deposit,
  - then Paper w/ Endorsement
- Scenario #2:
  - Multiple Mobile Deposits,
  - then Paper w/ Endorsement
- Scenario #3:
  - Mobile Deposit(s) with Blank Back (fake)
  - then Paper w/ Endorsement



# Restrictive Endorsements



- Purpose, as used in Reg CC...
  - To Indicate
    - Check has already been processed
    - Method of Processing
    - Restricted to a specific Depository Institution
  - To Prevent Duplicate Deposit of item
  - To Protect
    - RDC FI from Duplicate Claims
    - Payor





# Reg CC & Restrictive Endorsements



- **General Restrictive I**
- **General Restrictive 2**
- **Mobile Restrictive**
- **Virtual Only**

ENDORSE HERE

ONE NEVADA CREDIT UNION  
For Deposit Only

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE  
RESERVED FOR FINANCIAL INSTITUTION USE \*

Seq: 44  
Batch: 135299  
Date: 10/24/17

Seq: 00044 19/24/17  
BAT: 135299 CC: 336368549  
WT: 81 LIPS Dallas TX  
-BC: Boulder Horizon BC NVI-19

The security features listed below, as well as those not listed, exceed industry guidelines.

| Security Features:         | Results of document alteration:                                |
|----------------------------|--|
| Microprint Lines           | • 2D Small type in line appears as solid line when photocopied |
| Chemically Sensitive Paper | • Stains or spots may appear with chemical alteration          |
| Security Screen            | • All content of document is visible through security screen   |

\* FEDERAL RESERVE BOARD OF GOVERNORS REG. CC

ENDORSE HERE

FOR DEPOSIT ONLY  
MARK HARMON PEST CONTROL  
000058664228

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE  
RESERVED FOR FINANCIAL INSTITUTION USE \*

Seq: 44  
Batch: 135299  
Date: 10/24/17

Seq: 00044 19/24/17  
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\* FEDERAL RESERVE BOARD OF GOVERNORS REG. CC

ENDORSE HERE

For Mobile deposits only

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE  
RESERVED FOR FINANCIAL INSTITUTION USE \*

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\* FEDERAL RESERVE BOARD OF GOVERNORS REG. CC

ENDORSE HERE

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE  
RESERVED FOR FINANCIAL INSTITUTION USE \*

12/12/17 109417 464 316 CENLAR  
106413 4 1 >231272365< 0092803  
Credit the account of the within named payee  
Without prejudice PEG-REGULUS LA

The security features listed below, as well as those not listed, exceed industry guidelines.

| Security Features:         | Results of document alteration:                                |
|----------------------------|--|
| Microprint Lines           | • 2D Small type in line appears as solid line when photocopied |
| Chemically Sensitive Paper | • Stains or spots may appear with chemical alteration          |
| Security Screen            | • All content of document is visible through security screen   |

\* FEDERAL RESERVE BOARD OF GOVERNORS REG. CC

# Good, BUT...

# BETTER

# BETTER

**Appropriate Restrictive Endorsements require 2 minimum elements;**

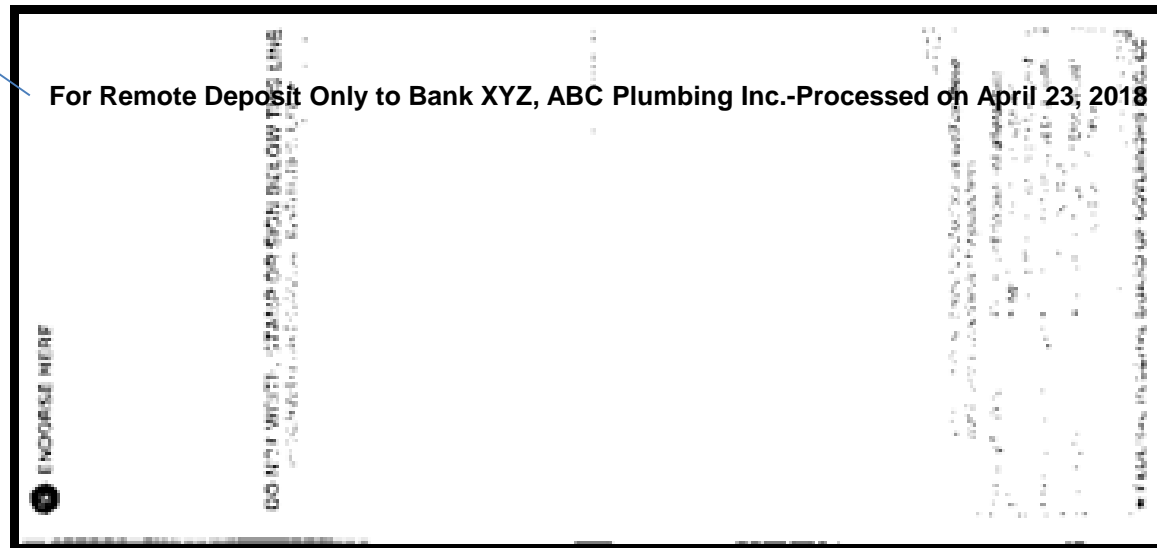
- 1) Method of Deposit (For Mobile Deposit Only)**
- 2) Intended Depository Institution (To Bank XYZ)**



# Scanner-Printed Endorsements?



**For Remote Deposit Only to Bank XYZ, ABC Plumbing Inc.-Processed on April 23, 2018**



**Key Question: Even if the depositor's endorsement is not in the "correct" location, is the endorsement still "valid" for the purposes of the Reg CC Indemnity?**



# Survey Results

## Reg CC Industry Readiness

John Leekley, [RemoteDepositCapture.com](http://RemoteDepositCapture.com)

54 Financial Institutions

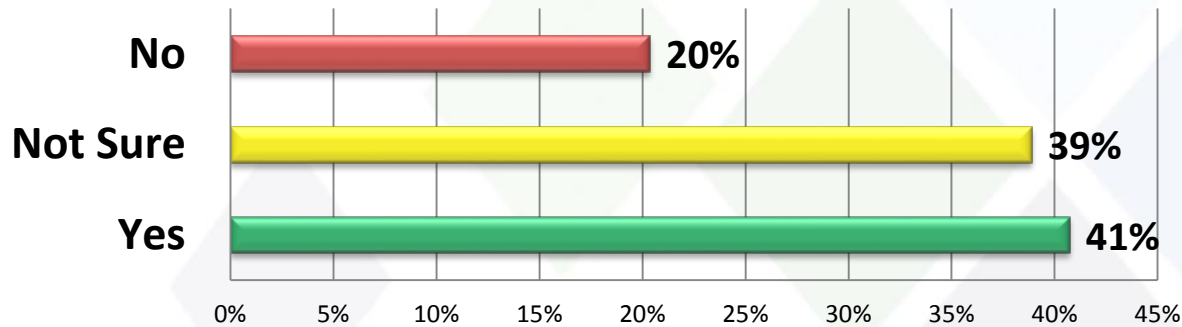
April 2018



# Most FIs Still Deciding on Changes

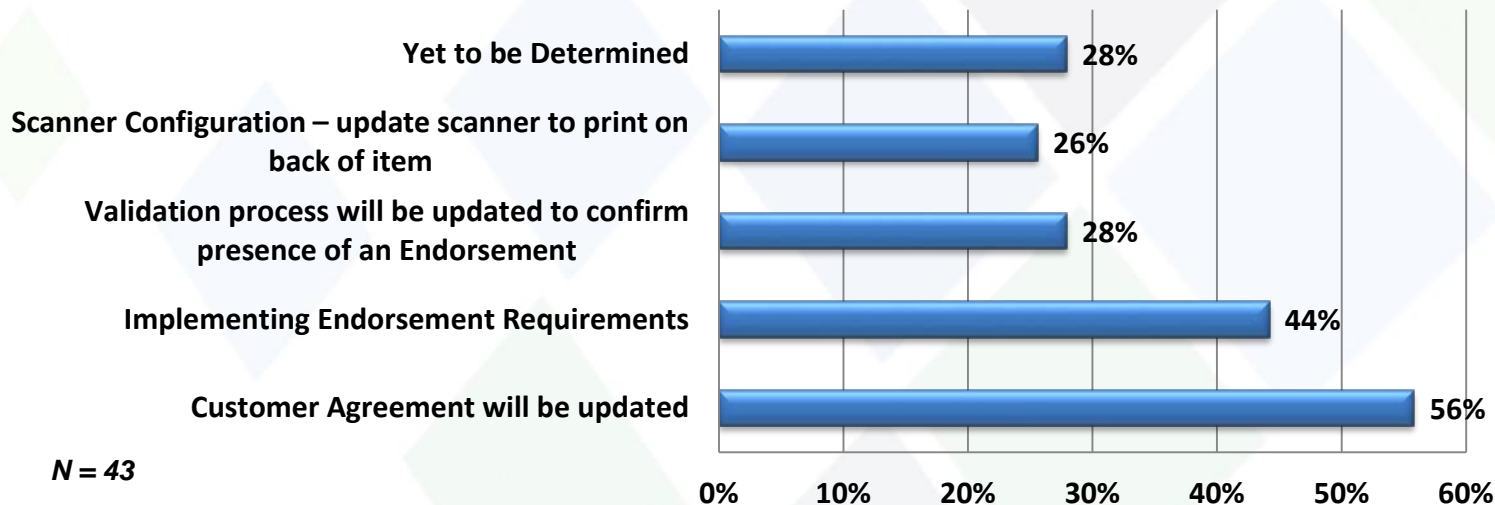


Are you making any changes to your Remote Deposit Program related to the upcoming Reg CC changes?



N = 54

In what areas will you be making changes?



N = 43

# Most FIs Require Specific Endorsements

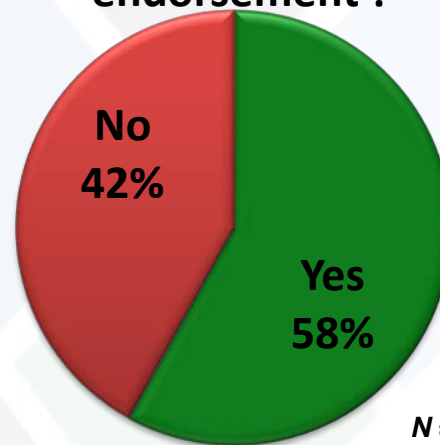


Do you currently require endorsements ?



N = 54

Do you require a specific restrictive endorsement ?

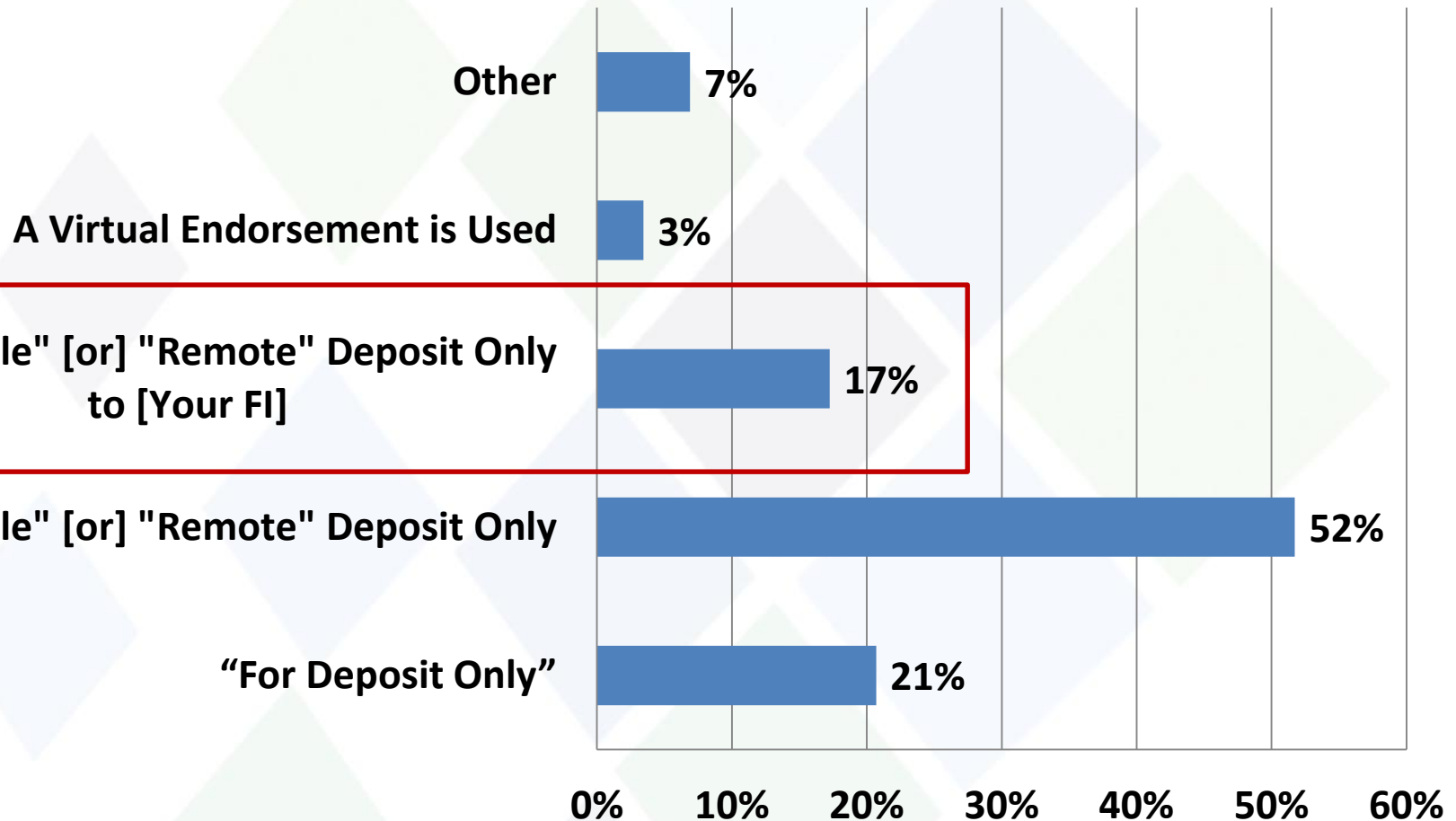


N = 50

# FIs Vary on Specific Endorsement Language



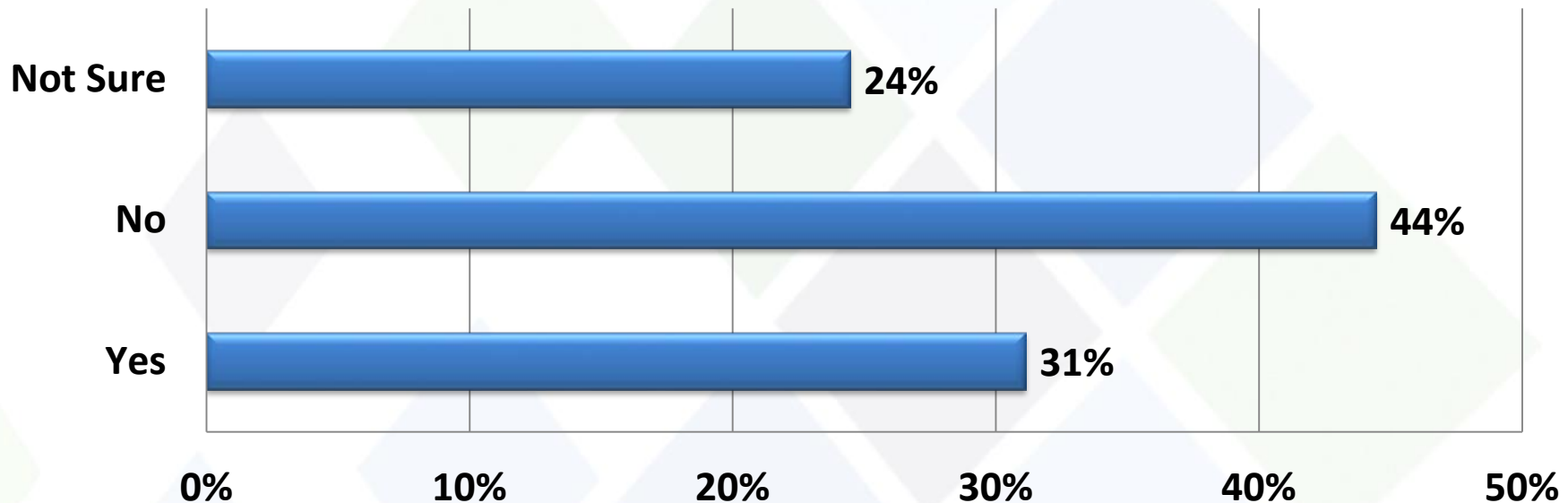
**What do you require the restrictive endorsement to say?**



# Automated Endorsement Detection is Low



**Can your current Solution identify the presence of an endorsement on the back of the item?**

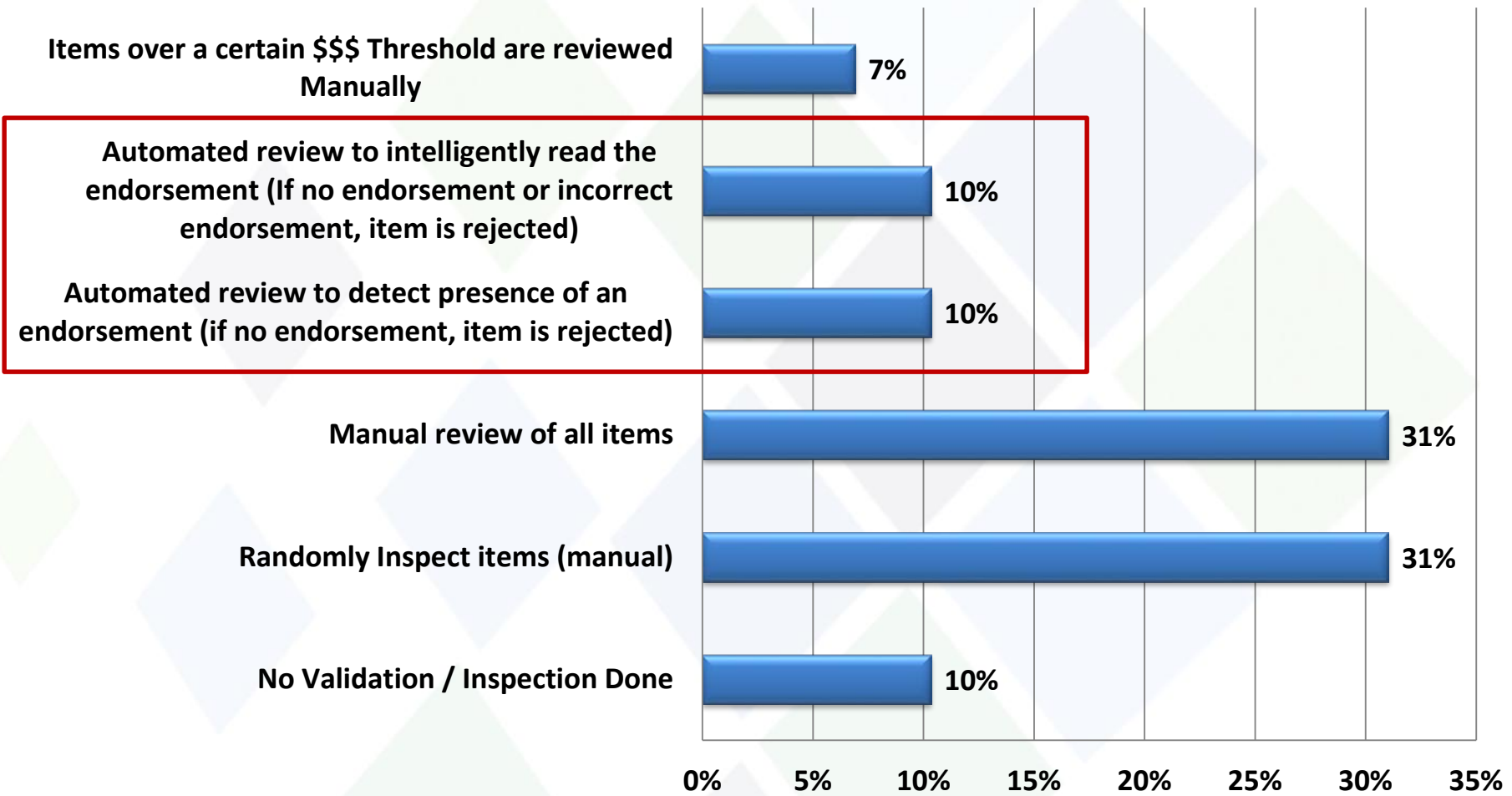


**Restrictive Endorsements have not been an important priority for most Solution Providers and Financial Institutions. But that's about to change...**

# Endorsement Review Process is Manual



How do you validate / Inspect the endorsement?





A decorative graphic on the left side of the slide, consisting of a cluster of diamond-shaped tiles in various shades of blue, green, and dark blue, arranged in a non-uniform, overlapping pattern.

# A Technological Approach to Restrictive Endorsements

Joe Gregory, OrboGraph

# Detection vs. Validation

## (Presence vs. Reading)

☐ ENDORSE HERE

*W. J. [Signature]*

**DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE**  
RESERVED FOR FINANCIAL INSTITUTION USE \*

☐ ENDORSE HERE  
 PAY TO THE ORDER OF  
 TO THE ORDER OF  
 DEPOSIT ONLY  
 CASH AND DEPOSIT  
 12/1/73  
 DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE  
 RESERVED FOR FINANCIAL INSTITUTION USE

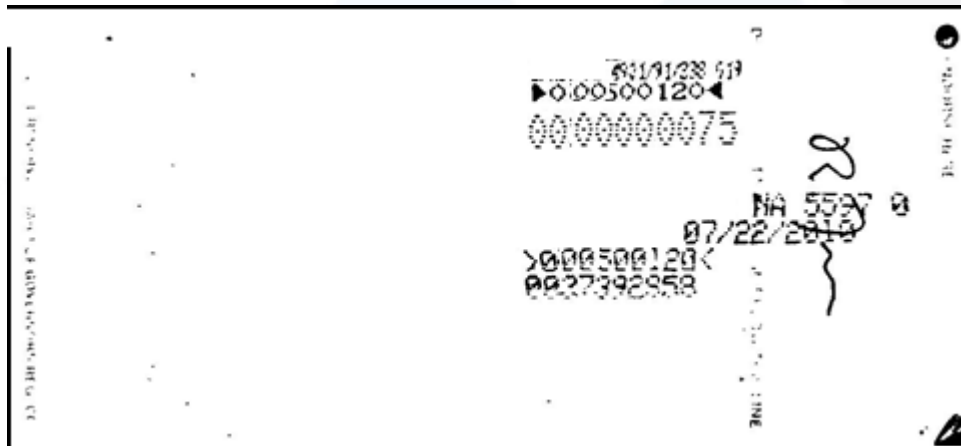
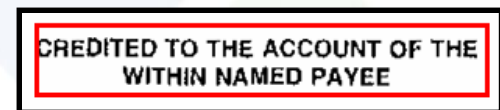
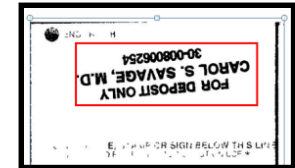
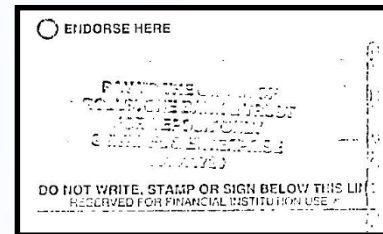
FOR DEPOSIT ONLY  
HEARTS IN MOTION, INC.  
115131710

DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE  
RESERVED FOR FINANCIAL INSTITUTION USE \*

# Challenges of Accurate Detection



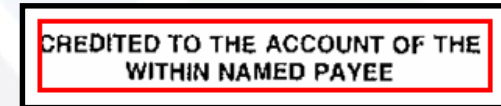
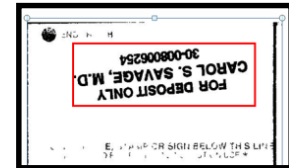
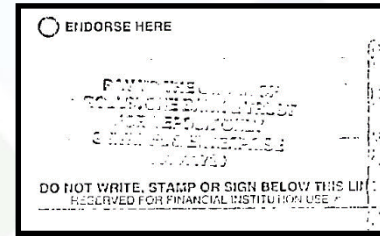
- Classification
  - Stamped vs. handwriting
  - Variability of endorsements
  - Quality
  - Placement
  - Virtual endorsement



# Challenges of Reading/Recognition



- Recognition
  - Keyword searching
  - Full field scoring
  - Matching vs. free read
- Technologies
  - OCR
  - ICR
  - Artificial Intelligence (Deep Learning)
  - Training



# Workflow Considerations



- Positive validation
  - Mobile RDC
  - RDC
- Negative confirmation
  - Teller
  - Branch
  - ATM
  - Kiosk
  - Inclearings: high dollar
- Check casher (MSB) deposits



# Validate Payment Negotiability To Match Your Deposit Agreement



- Is the amount correct?
- Is it post dated or stale?
- Does the payee match the account holder?
- Is it a 3<sup>rd</sup> party check or made to cash?
- Does the payor = payee?
- Does it match a negative list? Payee/payor/MICR
- Does a signature exist?
- Is it a money order or non-check?



# **Successful Automation**

**Leads to...**

**Customer Acceptance &  
Adoption**



# Key Lessons Learned - Endorsements



1. Restrictive Endorsements: NOT Required, but helps reduce risk of duplicates
2. Business Case: Labor, risk & fraud
3. To what level should EVERY item need to be inspected?
4. Recognition/AI Inspection:
  1. Solution providers developing enhanced solutions
  2. Banks still creating requirements



# Next Steps for your FI



- Update Legal Agreements
  - Use Appropriate Restrictive Endorsements
  - Ensure necessary changes for eligible items, Warranties, Indemnities
- Review Operations & Tech
  - New Return & Notice Requirements
  - Scanner Printing of Endorsements
  - Endorsement Review Process
- Work with your Solution Provider
  - Endorsement Presence ID & Verification
  - Endorsement Application (via Scanners)

# AGREEMENTS



- Electronic Presentment
  - Bilateral
  - Clearing House
  - Federal Reserve Regulation J
  - Operating Circular 3
- Remote Deposit Capture
  - Eligible Items (excludes ECI & RCC)
  - Endorsement Requirement
  - Indemnification
- Deposit Account
  - Item Includes
    - Checks, Drafts, Withdrawal Slips
    - Images
    - IRD
    - ECI
    - Electronic Debits (ACH, Debit Card, Online, etc.)
  - Remotely Created Checks (deposit and payment)



# Q & A



# Thank you to our Sponsor



For solution information on restrictive endorsement detection (Anywhere Validate) & check fraud detection

## Anywhere Validate

Validating payment negotiability of paper originated items

## Anywhere Fraud

Transaction and image analysis for counterfeit, forgery and alteration detection

- New resource page: [www.orbograph.com/reg-cc](http://www.orbograph.com/reg-cc)
- <http://orbograph.com/anywhere-validate/>
- <http://orbograph.com/anywhere-fraud/>



# For More Information



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