

BITS

FINANCIAL SERVICES
R O U N D T A B L E

**BITS VOLUNTARY GUIDELINES FOR COLLECTIONS
IN THE FINANCIAL SERVICES INDUSTRY**

MARCH 2004

A PUBLICATION OF THE BITS FRAUD REDUCTION STEERING COMMITTEE

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About BITS

BITS was created in 1996 to foster the growth and development of electronic financial services and e-commerce for the benefit of financial institutions and their customers. A nonprofit industry consortium that shares membership with The Financial Services Roundtable, BITS seeks to sustain consumer confidence and trust by ensuring the security, privacy and integrity of financial transactions. BITS works as a strategic brain trust to leverage intellectual capital to address emerging issues where financial services, technology and commerce intersect, acting quickly to address problems and galvanize the industry. BITS' activities are driven by the CEOs and their appointees—CIOs, CTOs, Vice Chairmen and Executive Vice Presidents—who make up the BITS Executive Committee and BITS Advisory Council.

The BITS Fraud Reduction Steering Committee was created to:

- Reduce payment and other financial-related fraud losses.
- Secure a critical mass of financial institutions to participate in a shared account database and standardized data collection process.
- Identify successful strategies for reducing check fraud and make those strategies available to the industry.
- Assess fraud risk exposure to electronification and develop strategies to minimize losses.
- Address industry issues related to identity theft.

Several working groups operate under the BITS Fraud Reduction Program. These groups include:

- **Collections Working Group** – Chair: Jim Regan, The Bank of New York Company
- **Debit Card/ATM Fraud** – Chair: Kevin Hale, BANK ONE CORPORATION
- **Electronification** – Chair: Dick Clausen, Bank of America Corporation
- **Identity Theft** – Chair: Joe Triano, Citigroup Inc.
- **Internet Fraud** – Chair: Gayle Helm, Wells Fargo & Company
- **Loan Fraud** – Co-Chairs: Scott Grizzle, SouthTrust Corporation and Lisa Zarzycki, Fifth Third Bancorp
- **Legal and Regulatory** – Chair: Maureen Wharton, J.P. Morgan Chase & Co.
- **Shared Databases** – Chair: Jan Otwell, J.P. Morgan Chase & Co.
- **Successful Strategies** – Chair: Peter Baldassaro, Hibernia Corporation

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THE BITS FRAUD REDUCTION STEERING COMMITTEE

Co-Chairs: Shirley Inscoe, Wachovia Corporation
Bob Jones, FleetBoston Financial Corporation

Collections Working Group

Chair: Jim Regan, The Bank of New York Company, Inc.

BITS Staff: Robin M. Slade

Participating Institutions

Allfirst Financial, Inc.
Bank of America Corporation
The Bank of New York Company, Inc.
BANK ONE CORPORATION
BB&T Corporation
City National Corporation
Comerica Incorporated
Fifth Third Bancorp
First Tennessee National Corporation
FleetBoston Financial Corporation
Hibernia Corporation
J.P. Morgan Chase & Co.
The PNC Financial Services Group, Inc.
SouthTrust Corporation
SunTrust Banks, Inc.
U.S. Bancorp
Wachovia Corporation
Washington Mutual, Inc.
Wells Fargo & Company

THE BITS COLLECTIONS WORKING GROUP

The mission of the BITS Collections Working Group is to reduce BITS member institutions' exposure to check-fraud losses related to altered checks and forged endorsements, and to improve the experience of consumers who fall victim to check fraud.

To accomplish this mission, the Working Group has created the Collections Contact List. The List opens lines of communication between financial institutions and helps support the escalation process by providing contact information for key collections representatives at participating institutions. Available only to institutions that contribute their contact information, the List contains the name(s) of those responsible for processing breach of presentment warranty claims for their respective collection departments. Organizations interested in participating should complete the form in Appendix B and submit it to BITS.

For more information, contact BITS Director Robin Slade at 773-973-0630 or robin@fsround.org.

I. EXECUTIVE SUMMARY

Check fraud is a growing industry problem. Nearly 20 percent of super-regional banks incurred more than \$20 million in check fraud-related operating expenses in 2001.¹ In order to enable the industry to resolve breach of presentment warranty claims expeditiously and in a way that is fair, accurate, and consistent, the BITS Collections Working Group created these processing guidelines, which apply to collection of altered, forged-endorsement, missing-endorsement and improperly endorsed items.

If put into common practice, these guidelines will help the industry to be more responsive to customer claims of alterations and/or fraudulent endorsements of checks, while protecting financial institution assets. The guidelines can also help institutions mitigate unnecessary expenses associated with processing breach of presentment warranty claims. The goal of the guidelines is to help improve the overall financial institution collections process for the benefit of both the industry and its customers.

¹ American Bankers Association, *ABA Deposit Account Fraud Survey Report* (2002).

II. OVERVIEW OF THE PROJECT

Project Organization

This document was developed under the direction of the BITS Fraud Reduction Steering Committee. Project participants are considered to be specialists in collections, and represent BITS member financial institutions.

Data Gathering

The data for this project was gathered by the BITS Collections Working Group and project team members from participating organizations. The teams volunteered to comment on the current practices and industry guidelines. The document was vetted with the BITS Fraud Reduction Steering Committee, which oversees all Fraud Reduction Program activities.

III. INTRODUCTION

Breach of presentment warranty claims are governed by Articles 3 and 4 of the Uniform Commercial Code (UCC). This law governs check issues, and states that when a check is deposited, the depositing customer warrants that he or she has clear title to the check, that it has not been altered in any manner, and that the endorsement is genuine. The UCC generally imposes a three-year period of limitations on claims for breach of warranties in connection with check collections, but local law and clearing house rules can alter the general rule. The actual time limit on a particular claim may also depend on, among other things, how many banks are in the collection and return chain.

When a customer makes a deposit with a financial institution, that institution is considered the “bank of first deposit.” In accepting the item for deposit, it is essential that an institution know its customer and that the institution have sufficient resources available in the event an item is returned as dishonored. (See Appendix A for an overview of “know your customer” practices drawn from the BITS white paper *Financial Identity Theft: Prevention and Consumer Assistance*.) The bank of first deposit reserves the right to charge back the customer’s account for any item returned for alteration (on average up to one year from the date of deposit) or forged endorsement (on average from one to five years from the date of deposit).²

Please note: This document applies to both domestic and international collections drawn on US banks.

² Please refer to state-specific codes for local chargeback timeframes.

IV. SERVICE LEVEL AGREEMENT

A. Overview

The length of time required to resolve a breach of presentment warranty claim significantly affects customer service and can unnecessarily increase financial institution expenses and exposure to fraud losses. To address these issues and improve working relationships between financial institutions, claims should be reviewed and responded to in a timely and efficient manner, regardless of circumstance.

B. Voluntary Guideline

Collection payment requests involving breach of presentment warranty claims should be reviewed and responded to within a maximum of 90 calendar days from receipt of the request. A valid response should be sent within the 90-day period, regardless of circumstance, including claims involving an unusual fact pattern that may delay the resolution of an item beyond the 90-calendar-day period.

V. AFFIDAVIT FOR COLLECTIONS

A. Overview

The collections process operates more quickly and efficiently when affidavits include all of the information necessary for processing. All affidavits need not look alike, however, it is suggested that they contain certain information to ensure the claim can be processed as expeditiously as possible.

B. Voluntary Guideline

Suggested elements to be included in the affidavit are:

- The claimant's complete name, address, home telephone number and business telephone number.
- The nature and type of claim. (Checkboxes may be provided.)
- A full and complete description of the instrument, including:
 - a. The account number and name on the account
 - b. The check number
 - c. The amount of the check
 - d. The payee's name
 - e. The signer's name (may be the same as the claimant)
 - f. The date of the item
 - g. The date the item was paid
- An explanation of the circumstances. (On altered claims, specify the altered fields and how they were changed.)
- Language binding the claimant to the prosecution process. (Sample: "I agree to testify or certify to the truth of all applicable statements in this affidavit before any judge, officer of a court, or other person, in any case now pending or which may occur regarding this affidavit.")
- An indemnification clause or declaration that the information is correct. (Sample indemnification clause: "I will indemnify and hold harmless [company name] and/or the bank where the check was negotiated or deposited from any liability arising out of, relating to, or in any connection with the claim in the event that the representations of fact made herein should prove untrue." Sample declaration: "I declare under penalty of perjury that the foregoing information is correct.")
- A declaration that the person did not authorize and did not benefit from the situation being reported. (Sample: "I did not receive any benefit or value from the proceeds of the fraudulent item(s), and no proceeds were applied to any use or purpose on my behalf.")
- A place for notarization, if required.

VI. AFFIDAVITS FOR MISSING ENDORSEMENT OR NOT ENDORSED AS DRAWN (RETURN WITHOUT ENTRY CLAIMS)

A. Overview

Financial institutions often require their customers to execute an affidavit when reporting a missing and/or improper check endorsement. This is in most cases an unnecessary inconvenience for the customer. Upon receipt of a breach of presentment warranty claim, the bank of first deposit can readily resolve issues of missing and/or improper check endorsement by identifying the depositing account and determining whether or not it is held in the payee's name. Since the check or draft either does not bear endorsement or bears an incorrect endorsement, an affidavit should not be required. Eliminating this extra step helps make the customer's experience simpler and easier.

B. Voluntary Guideline

Upon confirmation from the intended payee that he or she did not benefit from the proceeds of the check, affidavits should not be required in order to process a claim for a single payee item for missing endorsement or not endorsed as drawn (return without entry claims). However, because affidavits may be requested by the bank of first deposit for breach of presentment warranty claims involving an unusual fact pattern or circumstances, the financial institution should reserve the right to request an affidavit. For example, an affidavit may be required by an international correspondent bank for these types of claims, such as suspected fraud.

VII. NOTARIZATION OF AFFIDAVITS FOR FORGED ENDORSEMENTS AND ALTERATIONS

A. Overview

It is common practice at most US financial institutions to require affidavits of forged endorsements and/or alterations to be notarized. However, for financial institution customers, particularly those residing outside the US, obtaining a notarization can pose a significant burden. Some find they must pay extraordinary fees for notary services. For others, the US Consular office or apostille may only be available in major cities, far from where the person is located.

B. Voluntary Guideline

For forged endorsements and alterations, a signature verification of the payee, in lieu of a notarization, can be guaranteed by one of the following:

- **A bank where the person is a customer**
- **A bank of international standing**
- **A US Consular office**

Financial institutions should continue to require a US Consular office or apostille, with the exception of situations in which it is unduly burdensome to the customer. In those cases, the customer may go to the bank of international standing and obtain a document, on the bank's letterhead, that includes standard verbiage as appears in Section V of this document. Based on the amount and other factors, authentication is left to the discretion of the paying bank.

VIII. IMAGE/MICROFILM DOCUMENTS

A. Overview

In support of the banking industry's electronification efforts and the movement to a check image environment, breach of presentment warranty claims should not be denied based solely on the fact that the original instrument is not available. A legible image and/or microfilm copy of the instrument or image-replacement document (IRD) should be considered acceptable.

B. Voluntary Guideline

A legible image and/or microfilm copy of the instrument or IRD should be considered acceptable to support a claim for breach of presentment warranty. When a presenting bank provides such an image, together with an appropriate affidavit as described in Section V of this document, in the absence of any other valid defenses, the claim should be paid.

An exception should be made in cases where local regulatory requirements specify that the original document must be presented. Further, if a claim is denied, a specific reason for the denial should be provided.

IX. REASON FOR DENIAL

A. Overview

In order to improve resolution of breach of presentment warranty claims, claim denials should be specific and made in a timely manner.

B. Voluntary Guideline

If a breach of presentment warranty claim for forged endorsement or alteration that has been duly submitted is denied, the specific reason for the denial should be provided to the bank submitting the claim. The denial should be specific and conveyed to the presenting bank as soon as the determination is made, not to exceed the guidelines set forth in Section IV of this document. The denial should be made in accordance with the UCC.

The following are examples of denial reasons that are unacceptable if presented as the sole basis for denying a claim:

- The bank of first deposit cannot locate the payee or the payee does not agree with the claim. The disposition of the payee does not have bearing on the validity of the claim and cannot be used as a defense to deny the claim.
- The payee's account is closed or does not have sufficient funds to pay the claim, or the payee has filed bankruptcy. If a forged endorsement or alteration claim is submitted within the one-to-three year timeframe (number of years is based on UCC state-specific timeframes), the status of the payee's account is not relevant to the liability of the depositing bank to pay the claim.
- The original check is required. With the increased use of imaging and truncation of checks, original checks are not always available. A claim submitted with an indemnified photocopy of a check is considered valid and cannot be denied solely based on lack of the original check. (See Section VIII.)
- The original affidavit is required. If the original affidavit is lost in the mail, an indemnified affidavit is considered acceptable.

X. CLAIM ACKNOWLEDGMENT: TRACERS AND FAX-BACKS

A. Overview

Financial institutions can shorten breach of presentment warranty claim response times by ensuring claims are received by the bank of first deposit, reducing costs from telephone calls and postage, and reducing the time employees spend placing and responding to calls. Taking these steps should help improve processes for acknowledgement of and following up on claims, which directly benefits customers.

B. Voluntary Guideline

In order to eliminate tracers, financial institutions should:

- **Send fax-back forms along with each initial claim requesting verification of receipt of the claim.**
- **Agree, under normal circumstances, to wait 60 days before calling to request the status of the claim once receipt is verified.**

The form may be different for different institutions, but all forms should include the claim number at the bank of first deposit and the financial institution contact's name, phone number and email address. (Correspondence by email should be encouraged to promote efficiency.)

XI. CONCLUSION

These guidelines seek to improve service to the financial services consumer, while uniting the industry in improving its response to a problem all institutions face: check fraud. By enhancing the timely communication between financial institutions on breach of presentment warranty claims across the industry through a contact list, response-time SLA, and improved consistency in the use of affidavits, we will be better able to expedite claims and serve our customers. These guidelines will evolve as the industry moves to an image environment and electronic tools for communication are developed further.

APPENDIX A

KNOW YOUR CUSTOMER PRACTICES³

The USA Patriot Act, passed in October 2001, states that financial institutions must “implement reasonable procedures” upon opening new accounts to verify potential customers’ identities. Further, the Act states that records of the identification used during the verification process must be maintained and screened for affiliation with terrorist organizations. Know Your Customer (KYC) practices help organizations meet these new requirements and mitigate identity theft.

For account openings, institutions should take the following KYC-related steps:

- Maintain a customer identification program (CIP) with reasonable procedures for identifying any person, including businesses, to open an account.
- Maintain procedures for verifying the identity of customers (i.e., any signer) opening an account.
- Require information used to verify the customer’s identity to be retained. This includes the person’s name, address, date of birth, tax identification number, and other identifying information.
- Determine whether a customer appears on any lists of known or suspected terrorists issued by the federal government (through internal records and third-party vendors).
- Maintain firm policies for determining the point at which an account should not be opened because the person’s identity cannot be verified.

Customers should be properly identified using two acceptable forms of identification. Acceptable forms of identification are:

- Bank-issued ATM card or debit card.
- Driver’s license with photo (original, not duplicate). Includes US territories, such as Puerto Rico, as listed in the *ID Checking Guide* published by the Drivers License Guide Company. (These must be accepted with care since many do not contain the same security features as state licenses. Consult the *ID Checking Guide* for a description.)
- New Jersey non-photo driver’s license (original, not duplicate).
- State-issued learner’s permit with photo.
- State-issued non-driver’s ID card with photo.
- State, county, or city-issued senior citizen ID card with photo.
- Military ID card with photo.
- US or foreign passport with photo.
- Mexican consular ID card with photo.
- US Immigration and Naturalization Service (INS) issued Alien Registration Card with photo (includes Resident Alien and Employment Authorization Cards).
- State, county, or city-issued welfare/public assistance card with photo.
- Electronic Benefits Transfer (EBT) card with photo.
- Major credit card (American Express, Visa, MasterCard, Novus).
- New Jersey Casino Commission and Connecticut Casino Commission ID cards.

An exception may be made for a customer verified as a “known customer” with branch manager or designee approval. However, the institution must be able to prove that the person was at some prior time properly identified and verified in a way that meets the requirements of the regulation.

³ Excerpted from the BITS white paper, *Financial Identity Theft: Prevention and Consumer Assistance*, published June 2003. The white paper is available at www.bitsinfo.org/wp.html.

Compare the identification to the presenter. Determine the following:

- Does the picture resemble the customer?
- Is the date of birth reasonable?
- Do the eyes, hair and height of the customer match the description?
- Is the information on the identification (i.e., name, address, etc.) consistent with the information verbally provided by the customer?
- Is the identification provided consistent with the customer's situation? (For example, is a non-resident alien contradictorily presenting an INS-issued alien registration card or "green card"? Is a person born after 1943 presenting a senior citizen ID card?)
- What is the date of issuance? If the ID was issued in the last 60 days, be cautious. Recently issued identification is more likely to be fraudulent.

Examine both forms of identification to determine whether the information is consistent. If there are any discrepancies, ask the customer to explain. Proceed only if he or she provides a reasonable explanation, such as "I colored my hair when that picture was taken," "I've since moved after I obtained my driver's license," or "I changed my name after I married."

APPENDIX B

COLLECTIONS DEPARTMENT CONTACT INFORMATION SHEET

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COLLECTIONS DEPARTMENT CONTACT INFORMATION SHEET

Organizations wishing to receive a copy of the BITS Collections Contact List must first submit their collections department contact information. Please complete the following questionnaire and send it to Robin Slade, Director, BITS at robin@fsround.org or fax to 773-743-2501. Questions about the Contact List should be directed to robin@fsround.org or 773-973-0630.

ORGANIZATION NAME:

DEPARTMENT #1

Region:

Key Contact

Name:
Title:
Phone:
Fax:
Email:
Mailing address:

Secondary Contact

Name:
Title:
Phone:
Fax:
Email:
Mailing address:

DEPARTMENT #2

Region:

Key Contact

Name:
Title:
Phone:
Fax:
Email:
Mailing address:

DEPARTMENT #3

Region:

Key Contact

Name:

Title:

Phone:

Fax:

Email:

Mailing address: