


Top 10 Things To Know About UCC

Presented by:
Ellen Heffner, NCP

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Top Ten List

- 10 – Model Law
- 9 – Statute of Limitations
- 8 – Good Faith and Ordinary Care
- 7 – Negotiable Instrument
- 6 – Negotiation
- 5 – Stop Payments
- 4 – Customer Reporting of Unauthorized Signature
- 3 – Holder & Holder in Due Course
- 2 – Return Deadline
- 1 – Transfer & Presentment Warranties




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Uniform Commercial Code (UCC)

- Article 3 – “Negotiable Instruments”
 - Key provisions cover:
 - Definition and requirements of a negotiable instrument
 - Negotiation, transfer and endorsement of these instruments, and
 - Liability of the parties
 - Sample topics:
 - Transfer and Presentment Warranties
 - Standards of care required for processing checks
 - Establishing the identity of the payee
 - Negligence of maker in case of forgery or alteration
 - Forgery and fraud loss allocation
 - Holder in Due Course




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Uniform Commercial Code (UCC)


- ▶ **Article 4 – Bank Deposits and Collections**
 - **Key provisions cover:**
 - Check collection, payment, liabilities, time frames and responsibilities
 - Any provision under Article 4 may be varied by agreement between bank and customer, except:
 - Bank’s duty to “Act in Good Faith” and “Exercise Ordinary Care”
 - **Sample topics:**
 - Transfer and Presentment Warranties
 - When bank may charge customer’s account
 - Customer’s right to stop payment
 - Customer’s obligation to report unauthorized signatures
 - Statute of Limitations




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Number 10...



Model Law




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Model Law

- UCC Purpose: Standardized state laws that govern business and financial contracts
 - Establishes general duty standards for parties to **act in good faith** and **exercise ordinary care** in their transactions.
- UCC and revisions written by commercial law experts
 - Updates submitted as drafts for approval to National Conference of Commissioners on Uniform State Laws (NCCUSL)
 - Group now referred to as the Uniform Law Commission (ULC)
- **Model state law – Must be adopted by each state**
 - Enacted in all 50 states and District of Columbia, Puerto Rico, Guam and U.S. Virgin Islands
- Articles 3 and 4, together with case law, document legal boundaries for most aspects of check processing





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Number 9 . . .

Statute of Limitations






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Statute of Limitations


- Designed to prevent fraudulent / stale claims from arising after all evidence lost or after facts have become obscure through passage of time
 - Defense ordinarily asserted by defendant to defeat an action brought after appropriate time has elapsed
- UCC “model law” must be enacted by each state legislature
 - May either extend or reduce time limits, subject to certain restrictions
- Statute of Limitations: **3 years**




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NUMBER 8...



Good Faith and Ordinary Care




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Good Faith

- ✈ Defined in Article 1-201 (20) as:
 - Honesty in fact and observance of reasonable commercial standards of fair dealing
 - Common sense in business practice
 - Term is mentioned throughout UCC
 - Every contract or duty described within UCC imposes an obligation of good faith in its performance and enforcement
- ✈ UCC Article 4-103
 - Any provision under Article 4 may be varied by agreement; but the parties to the agreement may not disclaim a bank's responsibility for it's
 - Lack of Good Faith




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Ordinary Care

- ✈ Defined in Article 3-103 (9) as:
 - Observance of reasonable commercial standards
 - Applying the same level of care to all transactions
 - Term is mentioned throughout UCC
- ✈ UCC Article 4-103
 - Any provision under Article 4 may be varied by agreement; but the parties to the agreement may not disclaim a bank's responsibility for it's
 - Lack of Good Faith or
 - Failure to exercise Ordinary Care



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NUMBER 7...





Negotiable Instrument




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Negotiable Instrument




CHECK

- Draft
- Written Instruction
- Signed by the Drawer
- To Pay Fixed Amount of Money
- On Demand




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Negotiable Instrument

- Promise or order to pay
 - Order is a written instruction to pay money signed by the person giving the instruction
 - Must be a writing (physical item)
- Fixed amount of money
 - Value of the instrument
- Payable to bearer or to order
 - Payee
- Payable on demand or at a definite time
 - Date requirement
- Unconditional order
 - No other undertaking or instructions




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Negotiable Instrument

- ✈ UCC 3: Check Definition
 - Instrument is a “draft” if it is an order
 - Check definition can be found in UCC [3-104(f)]
 - Within negotiable instrument definition
- ✈ "Check" means a:
 - Draft: Payable on demand / drawn on a bank
 - Cashier's check or teller's check
 - Check even though described by another term
 - Ex: "money order"



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NUMBER 6 . . .



Negotiation




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Negotiation

- UCC 3-201 definition
 - "**Negotiation**" means a transfer of possession, voluntary or involuntary, of an instrument by a person other than the issuer to a person who thereby becomes its holder
- If an instrument is payable to:
 - **Identified person**: Negotiation requires transfer of possession of the instrument and indorsement by the holder
 - **Bearer**: May be negotiated by transfer of possession alone




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Negotiate a Check

➤ Considerations for checks to be negotiated:

- **Payee:** Check may be made payable to:
 - Named payee,
 - Payable to Cash
 - Blank
 - No identified Payee – Bearer instrument
- **Date:** Payable on demand or at will of the holder
 - If undated, the date is:
 - Date of its issue; or
 - Date it first comes into possession of a holder's
- **Fixed Amount:** Value that passes from account of Drawer to payee/bearer
 - Should appear twice on the check
 - Printed in numbers (courtesy/convenience amount)
 - Written in words (legal amount)
- **Signature of Drawer**
 - Authorizes the paying bank to disburse funds



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NUMBER 5...

Stop Payments




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Stop Payments

- Customer (or other person authorized to draw on the account) may:
 - Stop payment on item drawn on the account or
 - Close the account by an order to the bank
- Must describe the item or account with reasonable certainty
 - Order must be received timely to afford the bank a reasonable opportunity to act on it
- Stop-payment order is effective for **6 months**
 - Will lapse after 14 calendar days if original order was oral
 - Need to confirm in a record within that 14-day period
- Stop-payment order may be renewed for **additional 6 month periods**
 - Must provide record to bank while stop-payment order is effective
- Burden on customer to establish fact and amount of loss
 - If item is paid contrary to stop-payment order or order to close the account

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Stop Payments & Cashier's Checks

- **Cashier's check**
 - Bank is both drawer / drawee
 - Drawn on a bank
 - Signed by officer / employee of bank on behalf of the bank as drawer
 - Direct obligation of the bank
- **Declaration of Loss**
 - Declarer is the remitter or payee of the check
 - Declarer lost possession and cannot reasonably obtain possession of the check
 - Loss was not a result of transfer or lawful seizure
- **Obligated Bank**
 - Bank that issued the cashier's check
- **Claimant**
 - Person who claims the right to receive the amount of the Cashier's Check
 - Claimant is payee or remitter of the check

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Stop Payments & Cashier's Checks


- Claimant may file a **Declaration of Loss** for lost, destroyed or stolen cashier's check
 - **Claimant:** Assert the claim to bank that issued the cashier's check; and must
 - Describe the check with reasonable certainty
 - Request payment of the amount of cashier's check
- If claim complies with UCC provisions:
 - Claim becomes enforceable at **the later of:**
 - Time the claim is asserted, or
 - 90th day following date of cashier's check
- Until the claim becomes enforceable, it has no legal effect
 - Obligated (issuing) bank may pay the check
- When claim becomes enforceable
 - Obligated (issuing) bank becomes obliged to pay amount of check to claimant

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Number 4 . . .



Customer Reporting of Unauthorized Signatures


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Customers Duty to Report

- Customers Duty to Discover and Report Unauthorized Signature or Alteration (UCC 4-406(a)-(e))
- Bank that sends a statement of account must:
 - Return or make available to the customer paid items, or
 - Provide sufficient information to customer to reasonably identify paid items
- Customer must:
 - Exercise **reasonable promptness** in examining the statement; and
 - Must **promptly notify** the bank of unauthorized/altered item(s)
- If Bank proves customer failed to comply with these UCC review/notice duties, customer is precluded from asserting against the Bank the Customer's unauthorized signature or alteration on the item, if
 - Bank proves that Bank suffered loss by reason of customer's failure;
 - Unauthorized signature or alteration by the same wrongdoer on any other item paid in good faith by the Bank if payment was made before the Bank received notice from the customer




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Customers Duty to Report (continued)


- Statute of Repose (UCC 4-406(f))
 - UCC establishes a second preclusion for customer's failure to notify Bank of customer's unauthorized signature or alteration of item
 - Regardless of lack of care of either the customer or the bank, customer who does not within **one year** after the statement or items are made available, discover and report unauthorized signature or alteration
 - Customer is precluded from asserting against the bank the unauthorized signature or alteration
 - One year is the outside time limit for customer reporting of customer's unauthorized signature or alteration of item




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NUMBER 3...



**Holder
&
Holder in Due
Course**




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Holder

- UCC 1-201 (21) defines the Holder as:
- Person in possession of a negotiable instrument that is payable either to:
 - Identified person that is the person in possession; or
 - Bearer that is the person in possession




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Holder in Due Course

- **Holder in Due Course (HIDC) (UCC 3-302)**
 - Holder who has possession and took the item
 - In good Faith
 - For value
 - Without notice signature unauthorized or item altered
 - Without knowledge of claims against it
- **HIDC concept – Represents a “chain of ownership”**
 - No other payment system has this
- **Benefit of being the HIDC**
 - Can enforce item against drawer even if item was returned unpaid by drawee (Paying Bank)



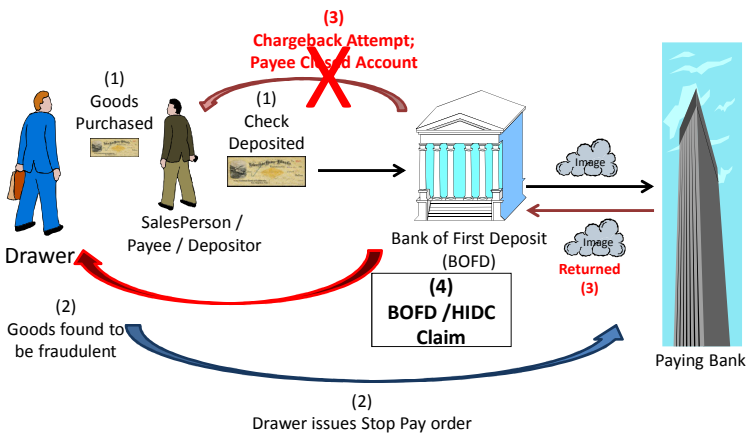
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Holder In Due Course – Example


- **Depository Bank (BOFD) is Holder In Due Course**
 - Can make claim back to Drawer






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NUMBER 2 . . .



Return Deadline




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UCC Provisions – Midnight Deadline

- With respect to a bank, this is midnight on its next banking day following the banking day on which it receives the relevant item
 - Represents timing required for Paying Bank to make a pay/no pay decision and get return out
- UCC 4-301: Return of items by payor bank
 - If Bank settles for a demand item, can recover the settlement if, before **its midnight deadline**, it
 - Returns the item; or returns an image of the item, or provides a notice of nonpayment





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*And the **NUMBER 1** thing to know about UCC. . .*

Transfer & Presentment Warranties





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Warranty and Indemnity in Payments

- Inter-bank exchange of checks subject to state/federal law
 - UCC, Regulation CC, Regulation J
- Rules and agreements important in assigning liability
 - Address exchange issues in uniform manner
 - Rules may be applied to exchanges across multiple financial institutions and exchange networks
- Check Image Rules
 - Establish legal rights and obligations of financial institutions in exchanging check images
 - Reduce risk to exchange participants




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UCC Transfer Warranties

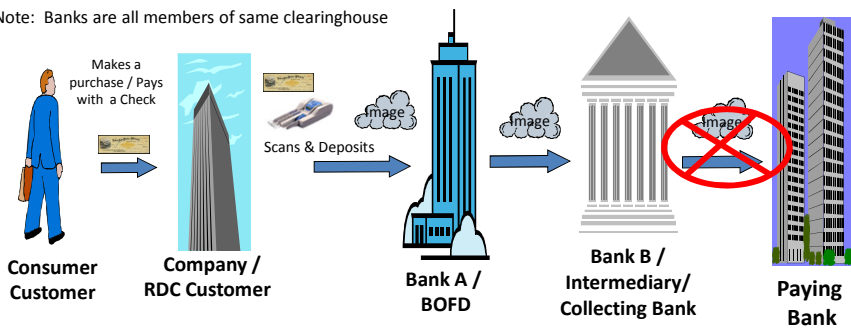
- ▶ Person or collecting bank transferring item warrants:
 - Entitled to enforce the item
 - **All signatures on the item are authentic and authorized;**
 - Item has not been altered;
 - Item is not subject to a defense or claim
 - Warrantor has no knowledge of any insolvency proceeding with respect to the maker
 - For a remotely-created consumer item, the person on whose account the item is drawn authorized item and amount for which the item is drawn

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UCC Transfer Warranties


Note: Banks are all members of same clearinghouse



▶ Does the UCC Transfer Warranty extend to the Paying Bank?


No – Stops with last collecting bank in the forward presentment chain

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UCC Presentment Warranties

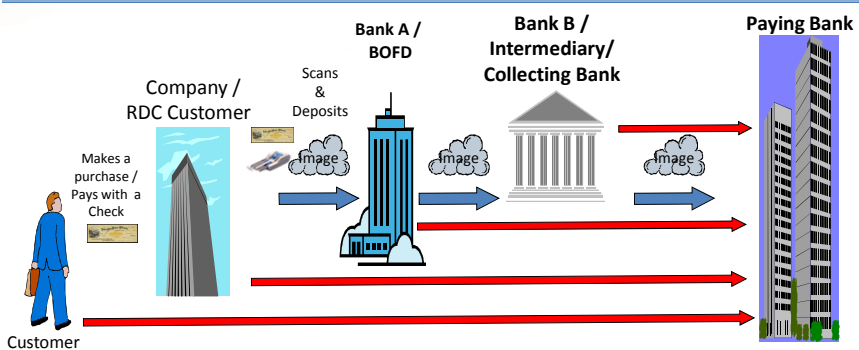
- ▶ Person obtaining payment and previous transferor presenting item warrants:
 - Entitled to enforce draft
 - Or authorized to obtain payment/acceptance of draft on behalf of a person entitled to enforce the draft;
 - Item has not been altered; and
 - **Warrantor has no knowledge that signature of the purported drawer of the draft is unauthorized;** and
 - For a remotely-created consumer item, person on whose account the item is drawn authorized item and amount for which it is drawn



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UCC Presentment Warranties




▶ Which institution receives the UCC Presentment Warranty?

Paying Bank



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Summary

- Inter-bank exchange of checks subject to both state and federal law
- Uniform Commercial Code provides standardized state laws that govern business and financial contracts
- UCC is model state law that is adopted by each state legislature
 - Versions are enacted in all 50 states and District of Columbia, Puerto Rico, Guam and U.S. Virgin Islands
- UCC Articles 3 and 4, together with case law, document legal boundaries for most aspects of check processing

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Recommended Resources

- Uniform Commercial Code (UCC)
 - Article 3 – Negotiable Instruments
 - Article 4 – Bank Deposits and Collections
- CheckImage Central Website:
 - www.checkimagecentral.org
 - White paper on “Need for rules”:
 - www.checkimagecentral.org/pdf/RoleOfPrivateSecRulesAndFRSRules.pdf


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THANK YOU!

***Ellen Heffner, NCP
Director***

eheffner@eccho.org

Electronic Check Clearing House Organization
3710 Rawlins Street; Suite 1075
Dallas, Texas 75219
www.eccho.org



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