

Canadian Cheques – Processing and Clearing

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Speaker Introduction

Session Overview

- Overview of Canadian Banking
- Canadian Cheque Image Evolution
- Status of Canadian FI Progress
- Characteristics of Processing
- Cross Border Exchange
- ECCHO Rules for Clearing Canadian items in U.S.
- Survey – What ECCHO Members are Doing with Canadian Image Clearing

Banking in Canada

- Banking in Canada is under Federal Jurisdiction
- A variety of legislation and statutes manage national banking
 - Bank Act: Defines 'bank'
 - Bills of Exchange Act: Defines 'cheque' and other payment instruments
 - Extended in 2007 to add image of a cheque as a Bill of Exchange
- Canadian Payments Act - Establishes the Canadian Payments Association, now called Payments Canada

Banking in Canada

- Payments Canada (www.payments.ca)
 - **IS** - The operating body that governs payments clearing and settlement in Canada at a national level
 - Manages the central settlement system (ACSS) for cheque and EFT
 - Manages the network for exchange of EFT and Image Captured Payment (ICP) files
 - **IS NOT** - A standards development organization
 - Provides standards specific to its mandate, supporting its members in participating in the national payments process and owns the standards
 - Cheques in Canada (30 min tutorial)
<https://www.youtube.com/watch?v=SDre9iWSgD8>

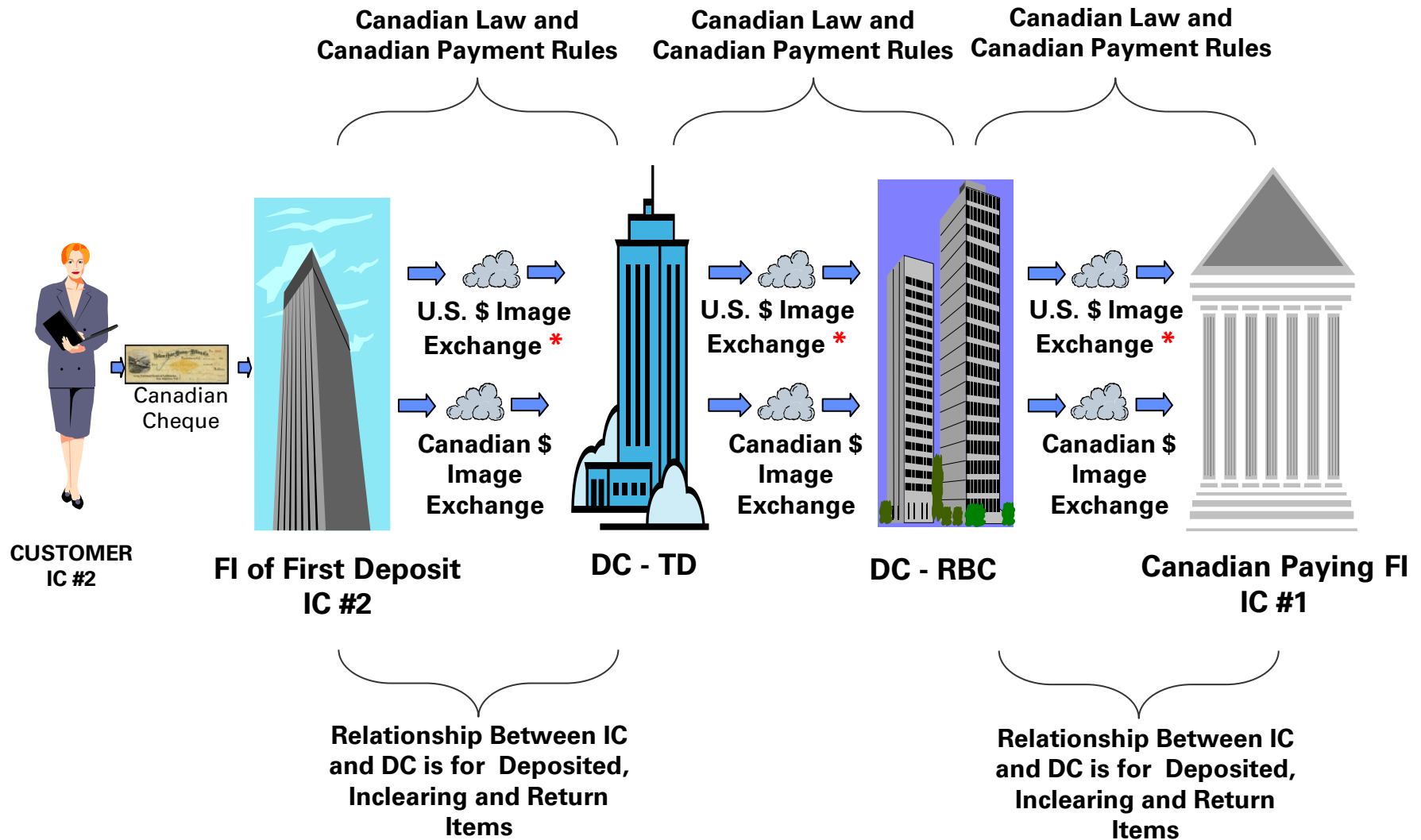
Banking in Canada

- Canadian Financial Institutions (FIs) are divided into:
 - ‘Direct Clearers’ (DC) and ‘Indirect Clearers’ (IC)
 - Direct Clearer (DC) – Participates directly in interbank exchange and settlement
 - Indirect Clearer (IC) - Contracts services of DC to represent it for exchange of other FI items that IC has taken for deposit
 - 12 Direct Clearers :

001: Bank of Montreal	039: Laurentian Bank of Canada
002: Bank of Nova Scotia	117: Bank of Canada - Receiver General
003: Royal Bank of Canada	(check issuer, no deposit taking, bonds)
004: Toronto Dominion Bank	219: ATB Financial
006: National Bank of Canada	815: Federation des caisses Desjardins
010: Canadian Imperial Bank of Commerce	du Quebec
016: HSBC Bank Canada	869: Central 1 Credit Union

- Approximately 100 Indirect Clearers

Banking in Canada



* Separate US ABA/Dollar from CDN Dollar

Cheque Image Evolution

- 2002 – 2008 - Truncation and Electronic Cheque Presentment (TECP) Project
 - Mandated exchange - ALL FINANCIAL INSTITUTIONS
 - Complex integration among/between direct clearers and indirect clearers
- Payments Canada Image Rule Project
 - **Phase I** – adopted **December 2009** – effective **June 1, 2010**.
Approved **Rule A10** (images of cheques) and **Rule A12** (image security standard)
 - **Phase II** – adopted **December 2010** – effective **June 1, 2011**.
Approved **amendments to Rule A10** related to creation and use of **Return Replacement Documents (RRD)**

Cheque Image Evolution

- Payments Canada Image Rule Project (cont'd)
 - **Phase III** – adopted **March 2012** – effective **October 1, 2012**.
Approved **amendments to Rule A10** related to creation and use of **Clearing Replacement Documents (CRD)**
 - **Phase IV** – adopted **June 2013** – effective **August 12, 2013**.
Approved **Final Rule amendments** to allow Direct Clearers to exchange electronic payment files containing Image Captured Payments (ICP) with partner that has agreed to participate in ICP Exchange
- Bilateral Agreements
- ICP Standard 015 – Companion Document to X9.100-187-2008

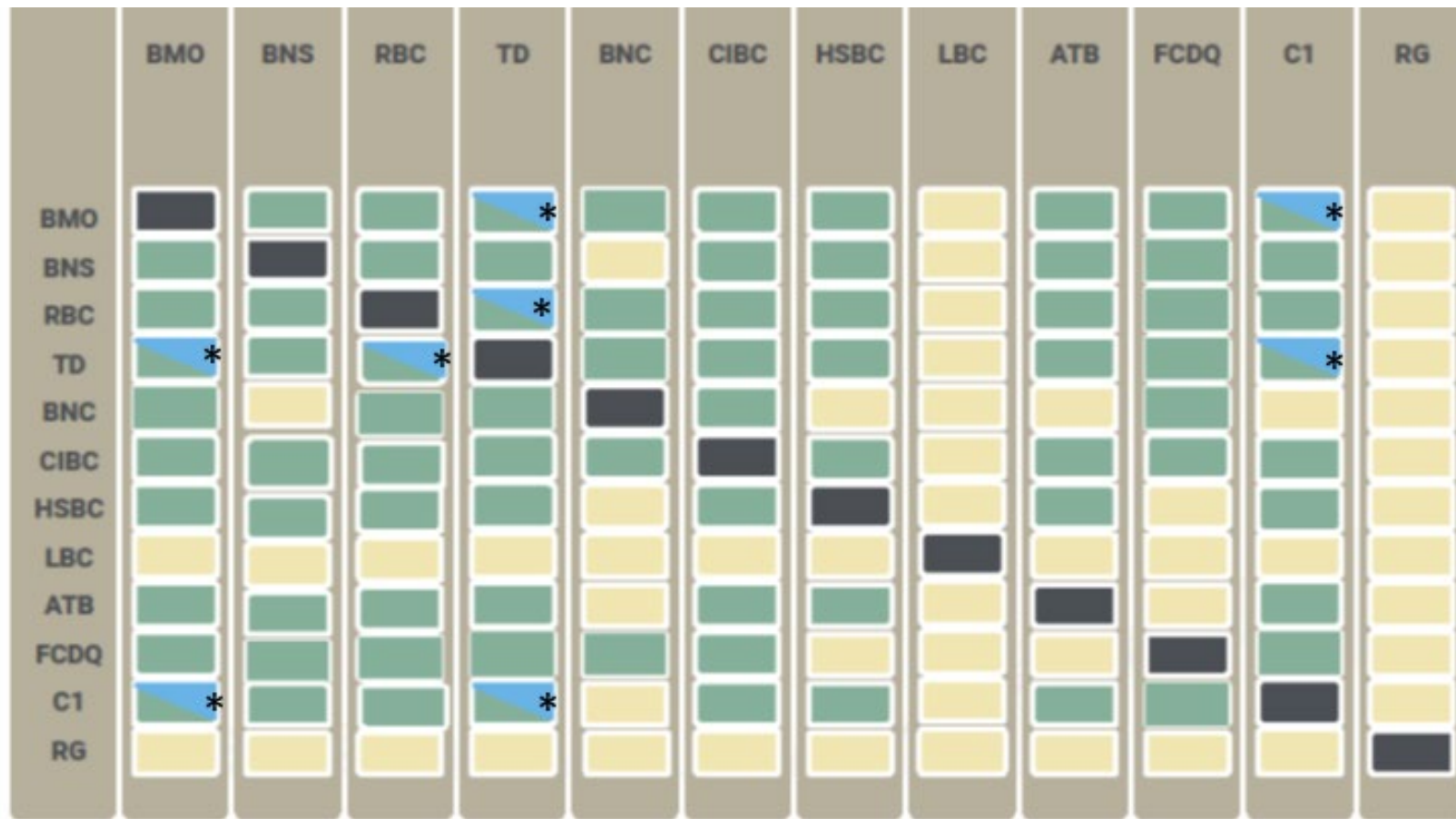
Cheque Image Migration Path

- Retain aspects of current process
- Develop New

- | | |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none">▪ Infrastructure Changes▪ Single Electronic Processing Site▪ Image Exchange Function▪ National Clearing (Optional)<ul style="list-style-type: none">• Cash letter per region included in one ICP (X9) | <ul style="list-style-type: none">▪ CRD and RRD Print Capability▪ All Source Capture Channels (RDC, Mobile, Branch, ATM)▪ Day 2 |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|

- Movement Away from Outsourcing
 - 3 of largest FIs moving to in-house
 - 2 of largest FIs moving to new outsource provider
 - Technical and, more importantly, Operational Impact

Cheque Image Exchange Migration Status



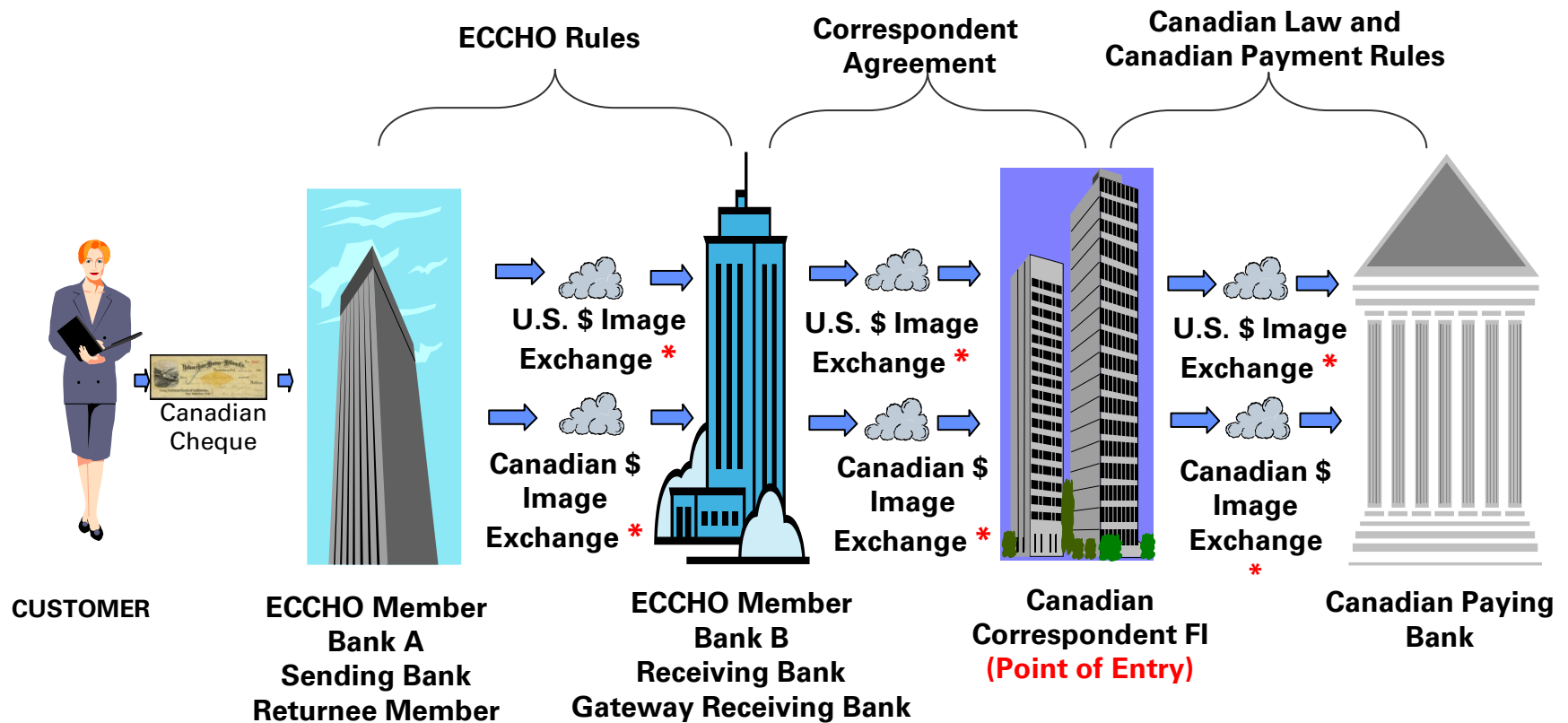
Updated as of September 8th,
2020



Bank of Canada does not participate in exchanges.
Receiver General is expected to begin receiving Q2 2021

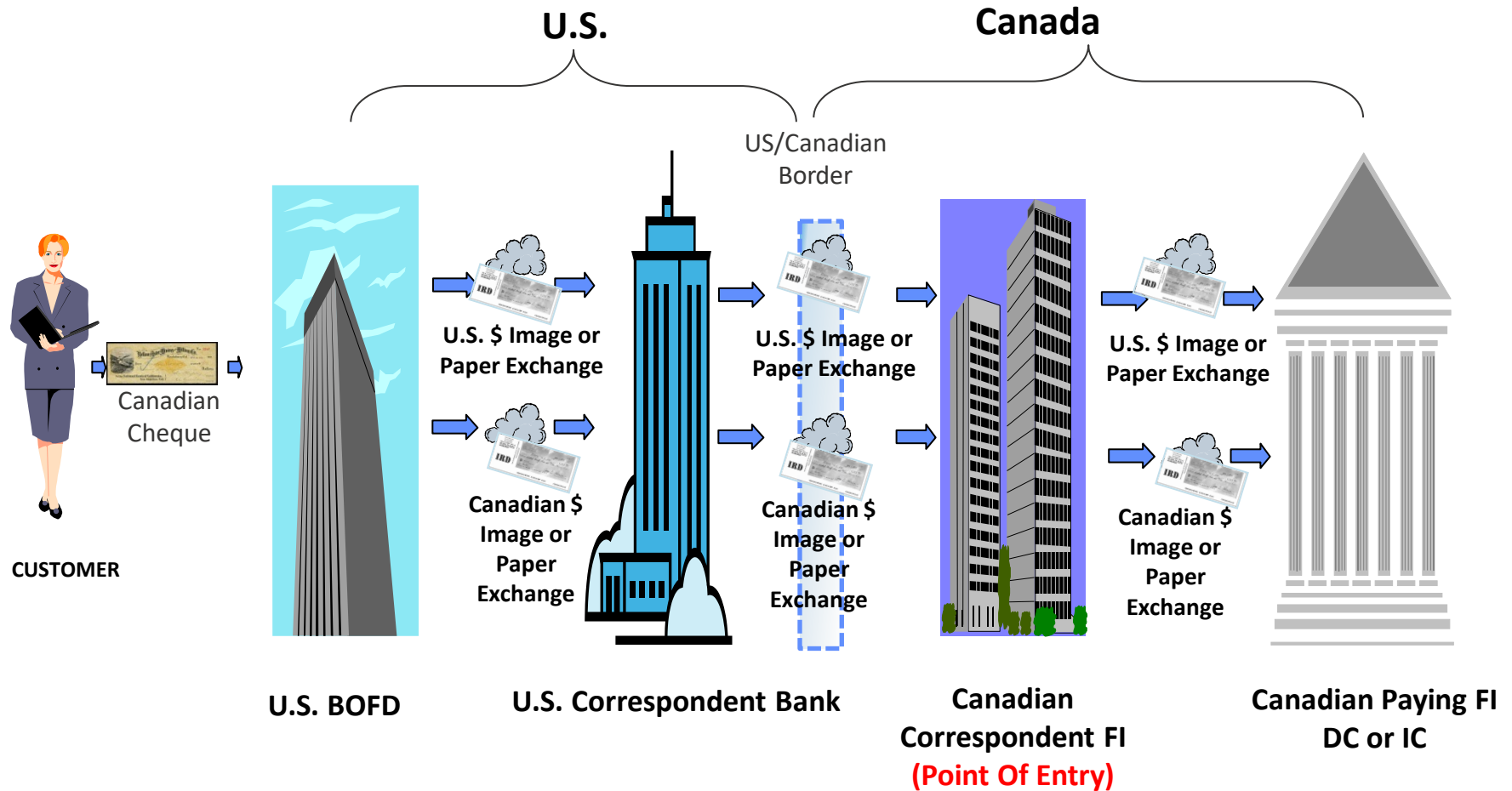
Cross Border Exchange - Overview

- Depositary Agreements with Canadian FI
- Exchange Rules/Depositary Agreements – within US
 - ECCHO Rules for clearing of Canadian Cheques



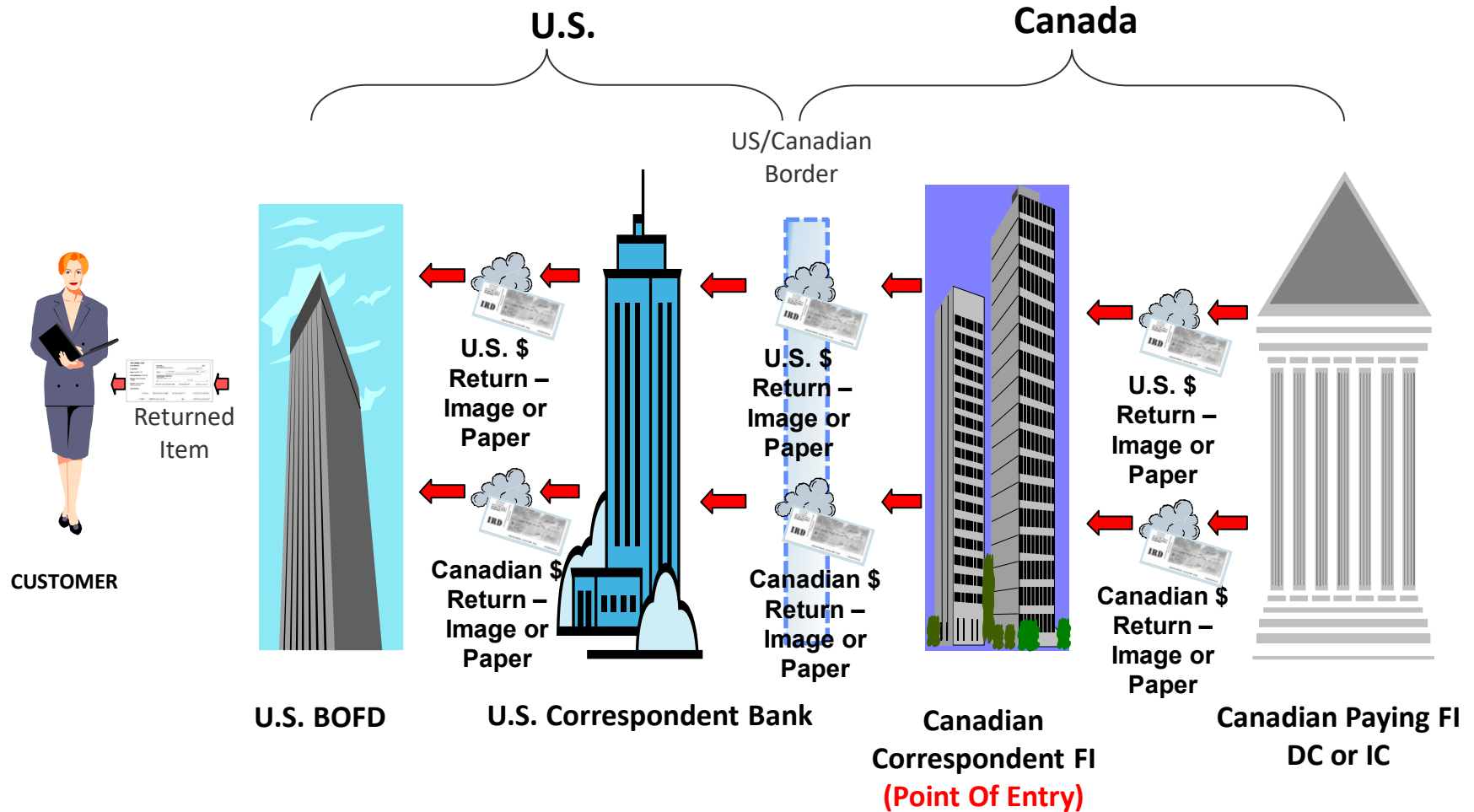
Cross Border Exchange

- Northbound Forward Exchange



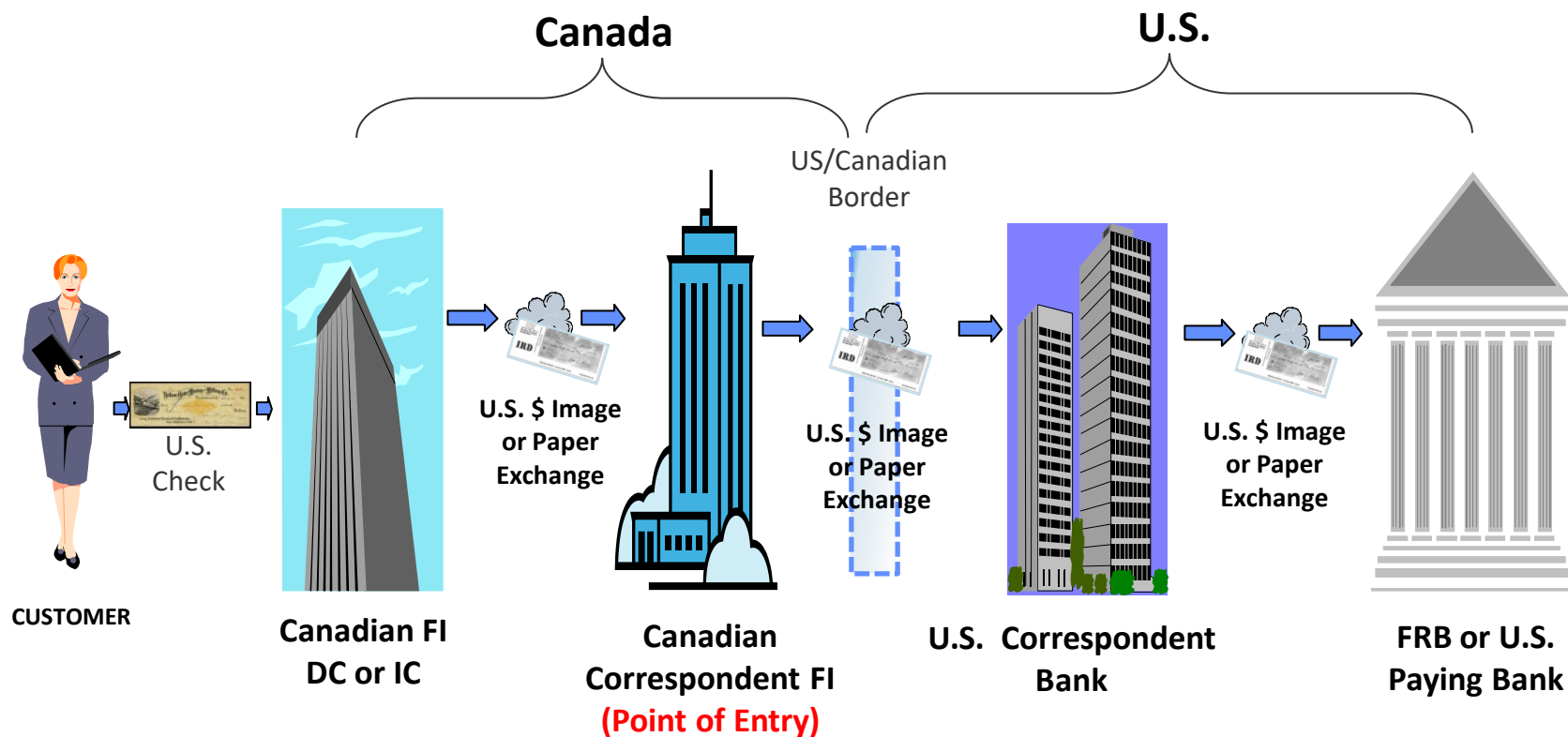
Cross Border Exchange

- Northbound Return Exchange



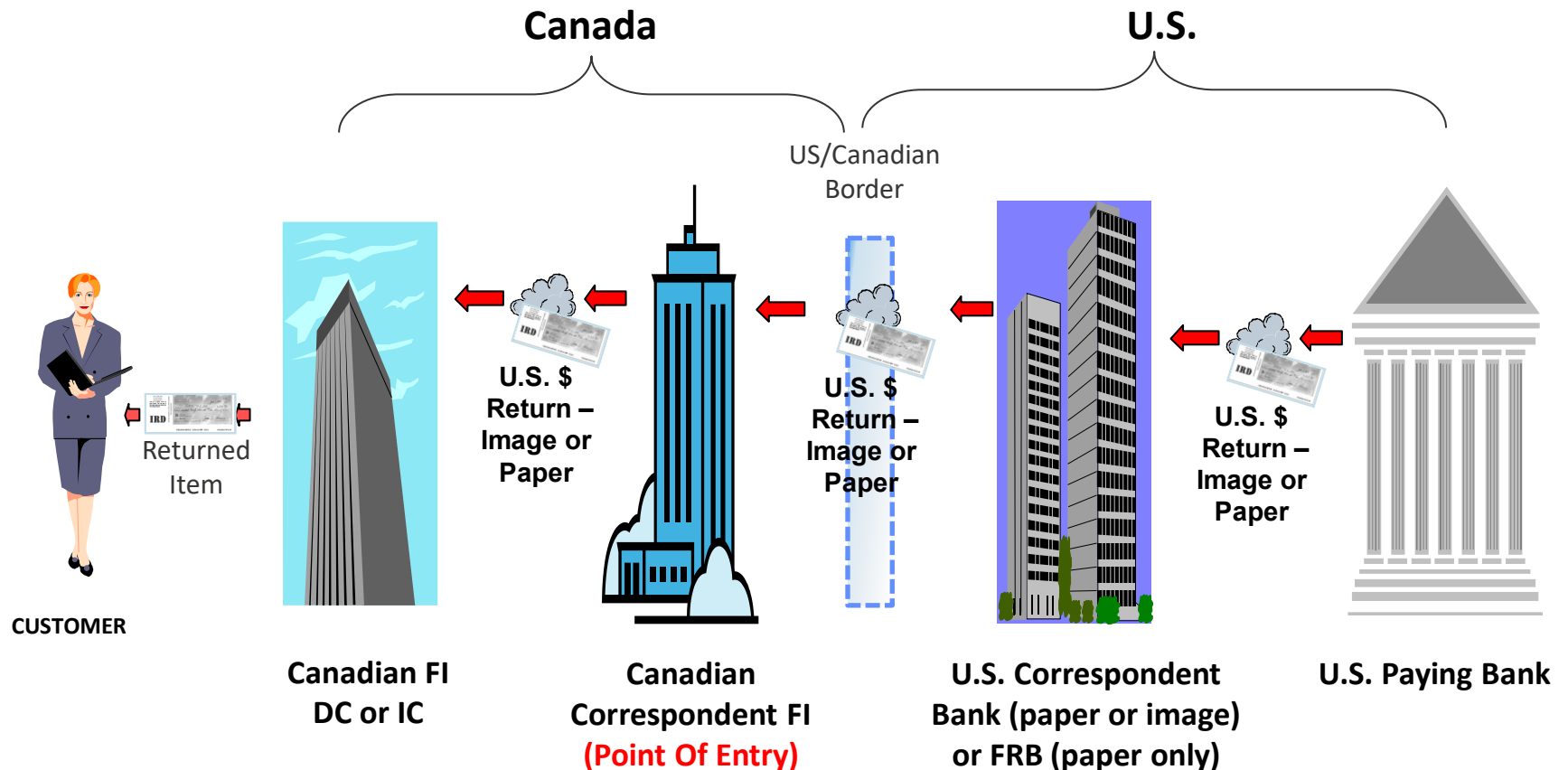
Cross Border Exchange

- Southbound Forward Exchange



Cross Border Exchange

- Southbound Return Exchange



Cross Border Exchange

- Processing Standards

- Northbound – Companion Document to follow Standard 015
- Southbound – Companion Document to follow X9.100-187
- Bitonal image – 200 dpi in tiff - standard to both countries

- R/T Format

- Retain “dash” in RT Field ex. 12345-010 In Record 25

- US Dollar vs Canadian Dollar Funded Accounts

- Both have XXXXX-YYY RT format
- US Dollar Funded Accounts – “45” in tran code field. See **Appendix A** for list of other characteristics
- Canadian Funded Accounts – “Hand-written” – US FUNDS
- Canadian Cheques without TC 45 will likely require operator review for proper designation

Cross Border Exchange

- Return Item Collection
 - Canadian FI Return Item Reason Codes **DO NOT** map directly with US Return Item Codes
 - US BOFD **cannot** represent returned Canadian cheque
 - Several conditions when BOFD can “re-exchange” Return Item (presented as first-time item)
 - Canadian FIs can return some categories of items up to 90 days and 6 years after presentment

Cross Border Exchange

- Return Item Collection – Reason Codes

United States		Canadian		
Description	Code	Code	Description	Time Limit for Return
NSF - Not Sufficient Funds	'A'	A	Insufficient Funds	
Stop Payment	'C'	B	Payment Stopped	
Post Dated	'H'	C	Post Dated	up to and including the due date
Stale Dated	'G'	D	Stale Dated	
Closed Account	'D'	J	Account Closed	
Altered/Fictitious Item/Suspected Counterfeit/Counterfeit	'N'	E	Counterfeit Item	
Refer to Maker	'S'	U	Refer to Maker	
Not Authorized (Includes Drafts)– Unauthorized item such as a draft	'Q'	K	Not Eligible for Clearing - Telecheque	90 calendar days
		K	Not Eligible for Clearing - Other	
Duplicate Presentment (Supporting documentation shall be readily available)	'Y'	N	Duplicate Payment	90 calendar days

See **Appendix B** for complete information

Cross Border Exchange

- Adjustments
 - An adjustment, as known in US, is not used in Canada
 - Canadian FIs enforce use of the Return process
 - ECCHO rules permits debit or credit adjustments to respective depositary account
 - ECCHO Adjustment code for adjustments within US

Overview of ECCHO Rules for Canadian Items

ECCHO Canadian Item Rules

- Members requested ECCHO Rules coverage for Canadian items
- Subcommittee formed
- Payments Canada and Canadian FIs participated
- Commentary includes:
 - Pertinent cases
 - Significant differences (i.e. returns)
 - Some Canadian law
- Rules approved (Section XVIII) effective August 3, 2015

ECCHO Canadian Item Rules

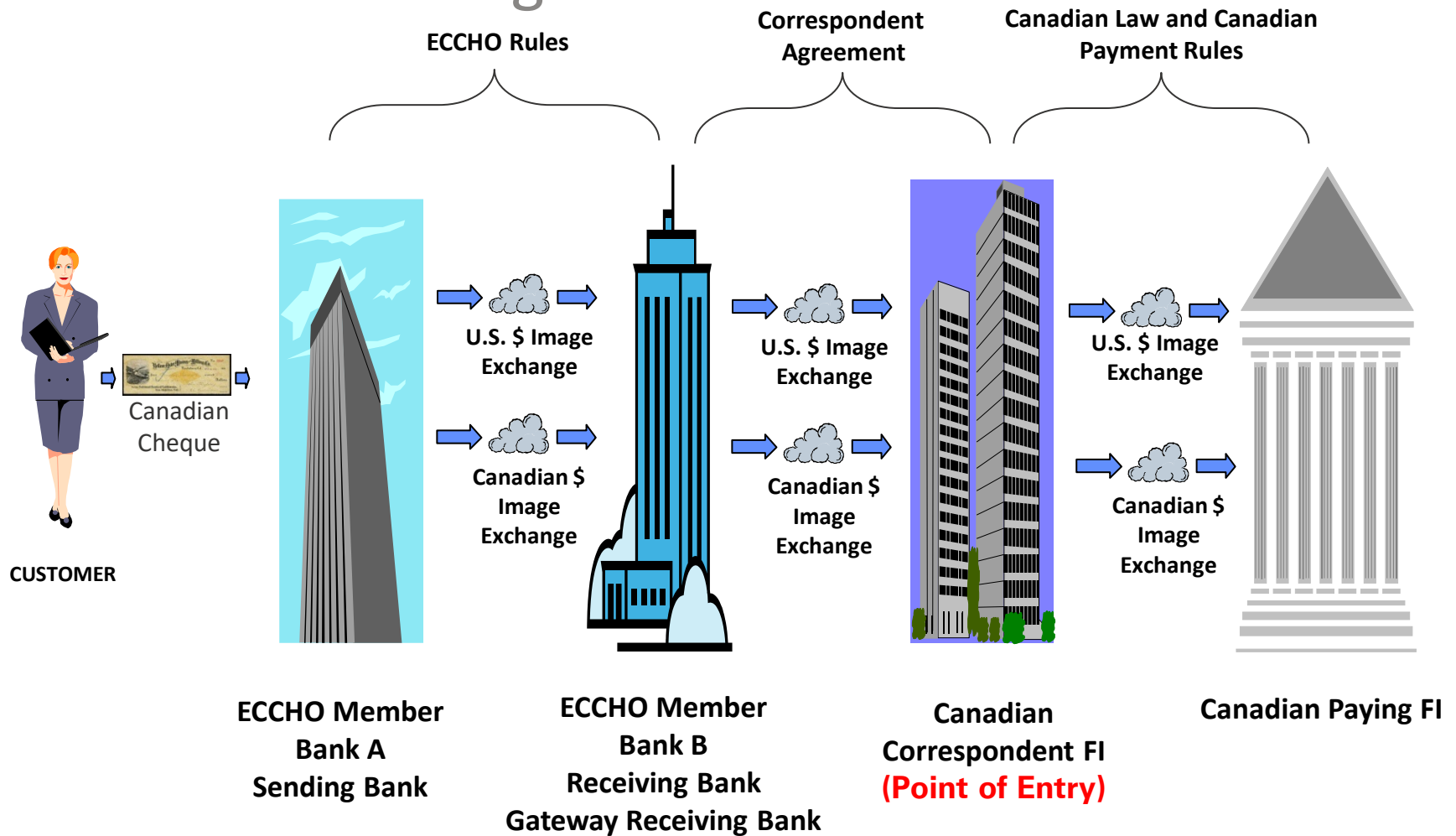
- New Definitions for Exchange of Images of Canadian Items (see Definitions section)
 - Canadian Law
 - Canadian Item
 - Canadian Correspondent FI
 - Canadian Paying FI
 - Canadian Paper Return Item
 - Gateway Receiving Bank

ECCHO Canadian Item Rules

- General Provisions – Application of Rules
 - Apply within U.S. for ECCHO member exchanges prior to exchange with Canadian FI - Northbound
 - Southbound exchanges of U.S. items already covered by ECCHO rules
 - Allowance for section to be varied by agreement
- Application of law to Canadian items
 - Canadian law applicable
 - Members responsible to understand applicable Canadian law
 - ECCHO Rules do not change Canadian law or rights under it
 - U.S. law applicable to obligations under Rules

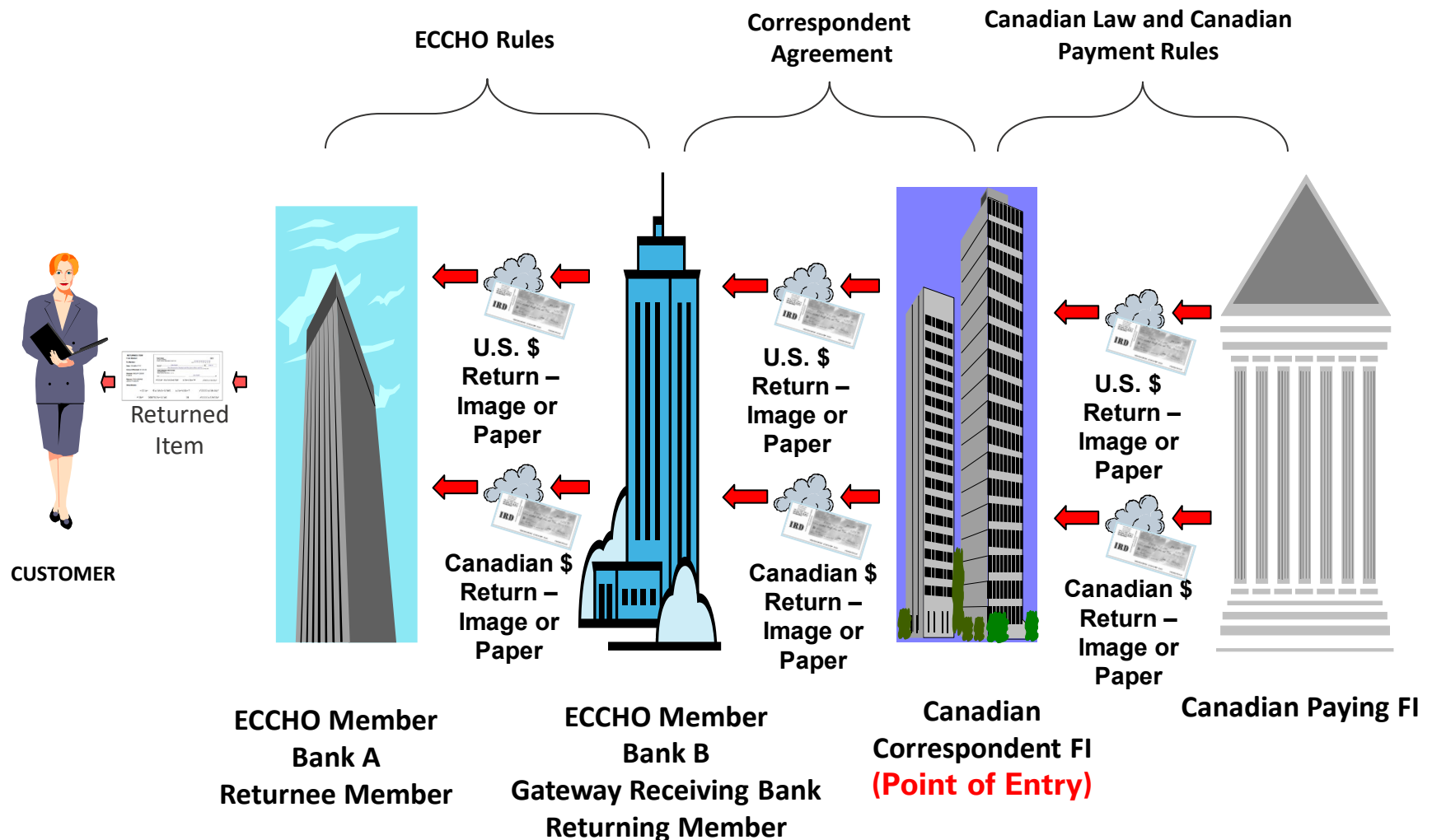
ECCHO Canadian Item Rules

- Forward Exchange



ECCHO Canadian Item Rules

- Return Exchange



ECCHO Canadian Item Rules

- Applies to Items eligible for exchange under Canadian Law
- Canadian image is “item” under UCC, not “check” under Reg CC
 - US Banks handle Canadian Image and Paper Return as collecting bank under Code
 - Provisions of UCC - Transfer warranties apply
- Destruction of Canadian Item within 120 days

ECCHO Canadian Item Rules

- Depositing customer agreement required
 - Responsible for check deposit relationship with customer
 - Review current terms of account agreement and consider needed changes
 - If RDC, destroy original cheque within 120 days
 - Rules do not cover RDC
 - Form of item that customer will receive for return
 - Prohibition of redeposit without permission
 - Reg CC availability does not apply to foreign cheques
 - Exchange Rate on Foreign Items

ECCHO Canadian Item Rules

- Separate electronic files for items of different currency
- Applicable Industry formats and standards required
- Gateway Receiving Bank may establish additional operational or formatting requirements
 - Based on its agreement with Canadian Correspondent FI
 - Responsible for exchange with Canadian Correspondent FI
- Image and Return RRD of Canadian Item is legal equivalent of Canadian item

ECCHO Canadian Item Rules

- Canadian Image Exceptions - Rejects, returns, correction or adjustment
 - Reg CC and UCC return timeframes do not apply
 - Can be returned or rejected by US or Canadian FI
 - May return Image or Canadian Paper RRD to FI that previously sent and maintain return reason codes
 - Return or reject sent to Member who originally transmitted or to another Member that agrees to receive return or reject
 - If Gateway Receiving Bank returns paper return, other Members maintain in paper form during return process
 - Subsequent presentment of returned items only if instructed or eligible under Canadian Law
 - Image can create an Official Copy of item

ECCHO Canadian Item Rules

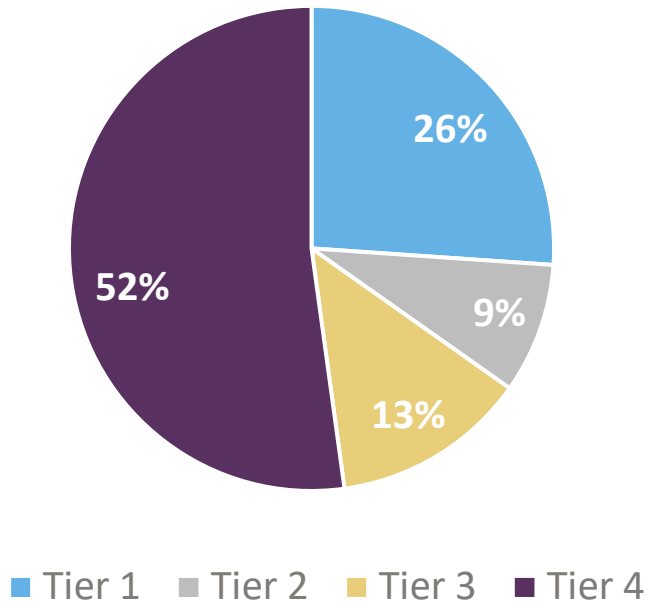
- ECCHO Adjustment Rules apply
 - Items are not handled as adjustments within Canada - expect returns and handle as adjustment in U.S.
- Cannot create Substitute Check from Canadian item
- Warranties and Indemnification
 - ECCHO warranties apply to Canadian image and Canadian Paper Return Item
 - Sending Bank indemnifies Receiving Bank except for its failure to exercise ordinary care or act in good faith
 - If Gateway Receiving Bank receives return warranty from Canadian FI, it makes same warranty
- Financial settlement for Canadian Items
 - No unique rules
 - Members may have separate settlement processes for currency exchange

Survey – ECCHO Members and Canadian Image Exchange

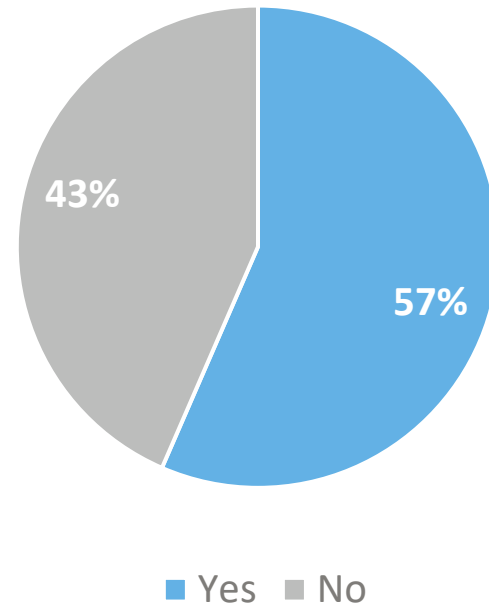
Saffici Payment Consulting was provided with the responses void of respondent name with a Tier level established by ECCHO

Survey – What ECCHO Members Are Doing

Survey Respondents by Tier

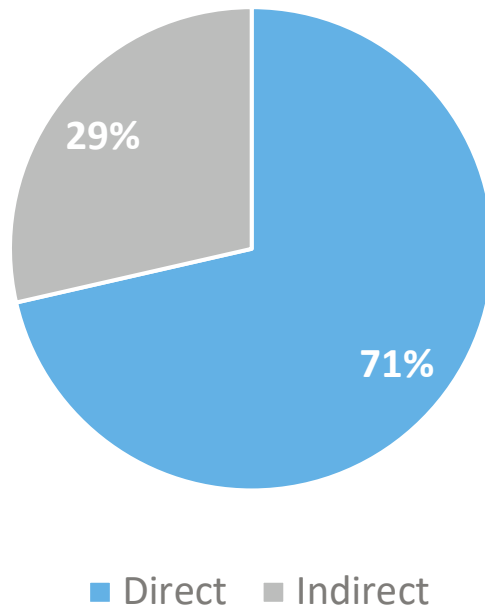


Respondents Clearing Canadian Cheques



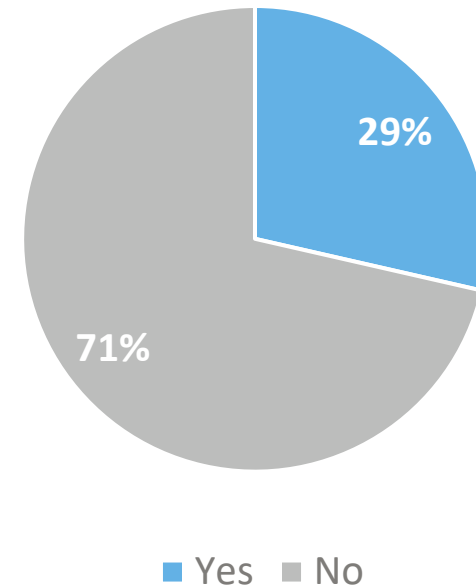
Survey – What ECCHO Members Are Doing

Respondents Clearing Direct with Canadian FI



3 Respondents clearing US Dollar Funded only
1 Respondent clearing CRDs converting to image

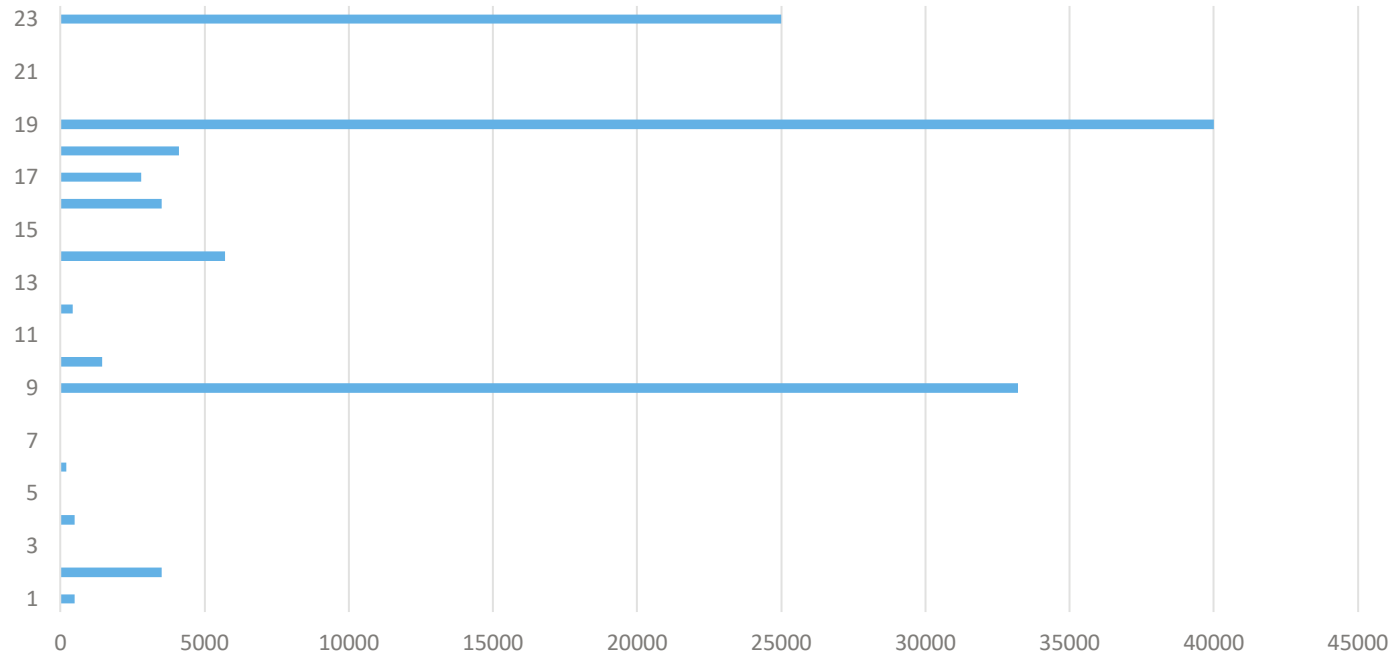
Respondent Offers Canadian Correspondent Clearing Service



1 Respondents has "grandfathered" correspondents only

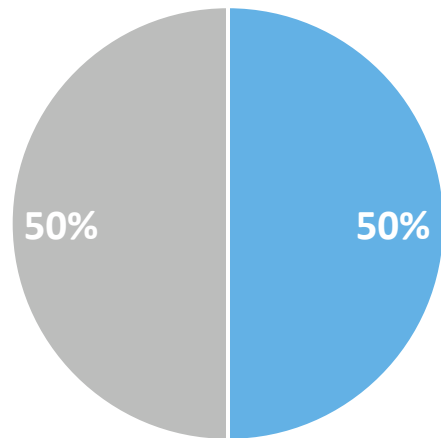
Survey – What ECCHO Members Are Doing

Average Monthly Volume - Respondents Clearing Canadian Cheques



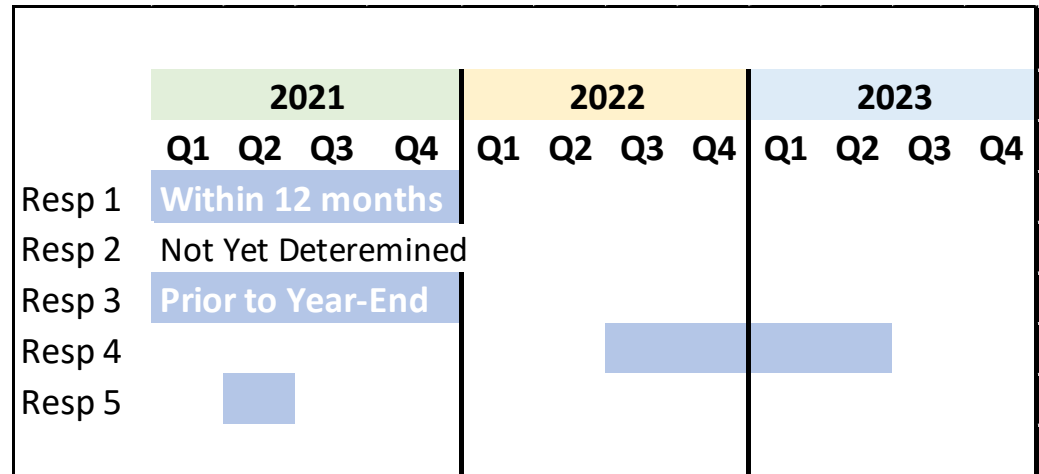
Survey – What ECCHO Members Are Doing

Respondents with Plans to Clear Canadian Cheques



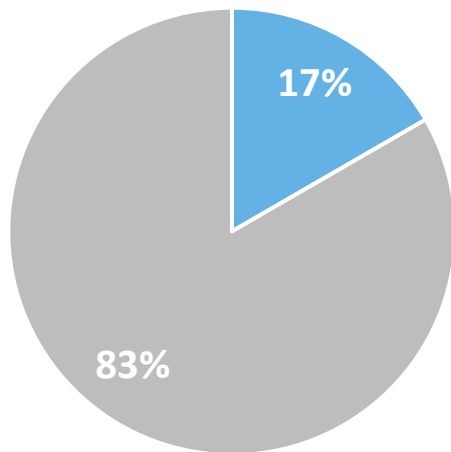
■ Yes ■ No

Timeframe To Implement Canadian Cheque Clearing



Survey – What ECCHO Members Are Doing

Receive US Checks (Image) from Canadian FI



■ Yes ■ No

Monthly Volume:
1 Respondent - 400,000 items

Survey – What ECCHO Members Are Doing

- Two Questions Were Asked of the Respondents:
 1. Please provide any **general technical or operational information relative to your preparation** for image-based Canadian Cheque Clearing that may improve industry efficiency of such clearing.
 2. Please provide any **general technical or operational information relative to your daily processing** of image-based Canadian Cheque Clearing that may improve industry efficiency of such clearing.

Survey – What ECCHO Members Are Doing

- Distinguish between US Dollar Funded Cheque and Canadian Funded Cheque
 - TC 45 is required on US Dollar Funded Cheques
 - Maker will write “US Dollar Funds” on Canadian Funded Cheque
 - Edit routine should examine for TC 45
 - Non-TC 45 items should be presented for operator review and TC 45 entered for those stating US Dollar Funds
 - Option to pre-sort physical items before capture and have designated capture routines. Difficult with teller and branch capture.
 - Examine your institution policy - when and how exchange rate affects customer

Survey – What ECCHO Members Are Doing

- Creation and Submission of ICL; Separate ICL Files by Dollar Denomination; ICL File Format
 - Canadian RT Validation
 - Proper identification of items (see prior slide)
 - File format - Northbound items will follow the Canadian Standard 015, which is a Companion Document to X9.100-180-2008
 - Agreement with FI that you are presenting to (Canadian FI or US Correspondent) will provide specifications.
 - NOTE: There is no standard among Canadian FIs regarding the file format of Northbound items. Ensure that you understand their requirement in how they address “deposit” X9 files, specifically credit record (Type 25 or Type 61).

Survey – What ECCHO Members Are Doing

- Northbound Return Items
 - Highly probable to receive in paper form – RRD (Return Replacement Document)
 - Return Reason Codes DO NOT map to US Return Reason Codes
 - Wrong Currency - high percentage
 - CANNOT represent items

Survey – What ECCHO Members Are Doing

- Daily Exchange Rate
 - Applying exchange rate to depositing customer
 - At time of deposit or back office
 - How is this coordinated with the cash letter amount presented either to the Canadian FI or US Correspondent Bank for settlement?
 - How is the exchange handled when an item is returned?

Q & A Discussion



Appendices

Appendix A – Canadian Currency

- The following excerpts contain more specific information on the identification of the various currency designations when dealing with Canadian cheques
 - Standard 006 – page 29 “Payable through U.S. Dollar”
<https://www.payments.ca/sites/default/files/standard006eng.pdf>
 - Standard 006 – page 53 “Transaction Code Section”
<https://www.payments.ca/sites/default/files/standard006eng.pdf>

Appendix B – Return Items

- Understanding Canadian Return Reason Codes

<https://www.checkimagecentral.org/-/media/cic/documents/understanding-canadian-return-reason-codes-update-2021-01-23.pdf>

- Content:

- “Code Match” - shows “side-by-side” US and Canadian Return Reason
- “Reason Match” – shows return reason codes that have same/similar meaning and identifies those with extended return times and manner by which the return can be presented
- “Re-Exchange Matrix” - shows the return reasons eligible for presentment as a new item (not representment)

Appendix C – Canadian Rules

- All Canadian Rules and Standards can be found at

<https://www.payments.ca/about-us/our-systems-and-rules/retail-system/rules-and-standards>

- The specific rules and standards applicable to this presentation are:

- Payments Canada Standard 015 (August 17, 2020) - Canadian Companion Document to X9.100-187 (2008) for Electronic Exchange of Canadian Cheque Images

<https://www.payments.ca/sites/default/files/standard015eng.pdf>

- Payments Canada Rule A4 - Returned and Redirected Items (April 27, 2020)

<https://www.payments.ca/sites/default/files/a4eng.pdf>

- Payments Canada Rule A10 - Image Rule (January 2, 2021)

<https://www.payments.ca/sites/default/files/a10eng.pdf>

Appendix D – Statistics

- Payment items settled through the Automated Clearing Settlement System (ACSS)

Payment item		2019	2018*	2017	2016	2015	2014	2013	2012
Cheques and paper items	Volume	467,054,748	510,833,402	553,244,377	599,371,256	658,084,133	715,259,219	769,336,925	814,767,640
	Annual Change	-8.6%	-7.7%	-7.7%	-8.9%	-8.0%	-7.0%	-5.6%	
	Cummulative Change	-42.7%	-37.3%	-32.1%	-26.4%	-19.2%	-12.2%		
	Value (\$000)	2,868,976,753	2,947,829,946	3,039,748,141	2,986,314,735	3,035,540,453	2,989,156,268	2,947,635,110	3,002,265,777
	Annual Change	-2.7%	-3.0%	1.8%	-1.6%	1.6%	1.4%	-1.8%	
	Cummulative Change	-4.4%	-1.8%	1.2%	-0.5%	1.1%	-0.4%		

Note: These volumes reflect all items processed, including On-Us items which are not cleared to another FI.

Appendix D – Statistics (Cont'd)

- Canadian Payments: Methods and Trends 2020

https://www.payments.ca/sites/default/files/paymentscanada_canadianpaymentsmethodsandtrendsreport_2020.pdf

- On-Us cheque volume 2019 vs 2018 – (-12%)
 - Business Cheques (-16%) Consumer Cheques (-5%)
- Percent of Total Remote Payment Volume
 - 2019 = 12% vs 2014 = 27%
- On-Us cheque value 2019 vs 2018 – (-7%)
- Percent of Total Remote Payment Value
 - 2019 = 39% vs 2014 = 51%

Thank You



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Thank You!

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