

Federal Reserve System Board of Governors
Request for comments: RIN 3064-ZA49
Payment Fraud

Concerning check fraud – this area of fraud has increased tremendously over the past five years. At first, it targeted business customers and now it is trending towards consumer customers.

Regardless of the type of account, the 48 hour deadline for customers to report these items to financial institutions to be returned is very unrealistic and impossible. In 85% of our check fraud cases, the item was mobile deposited at very large national banks.

- 1) Check law is far behind the times where technology is concerned. Although there is a movement to eliminate “paper” with a society relying on cards and electronic payments, checks are still being written. It is no longer realistic to determine in such a short time frame whether a check converted to an electronic image is legitimate. Check law should be updated to keep up with the times.
- 2) If a check is fraudulent, altered, or counterfeit and is a mobile deposit, the bank of first deposit (BOFD) should be held liable. Mobile deposits have allowed altered, counterfeit, and checks without MICR ink to be introduced to the system. Unlike transactions performed in person, the original source document is not viewable or present to be inspected. In addition, the BOFD has first chance at determining if the check is fraudulent based on when the account was opened and what is normal for their customer activity.
- 3) Community banks should not be financially burdened with legal expenses arising from baseless claim denials by larger national banks. In 2019, the Federal Reserve Board amended UCC to clarify the burden of proof when there is a dispute as to whether a substitute or electronic check has been altered or is a forgery. If there is a dispute about whether a substitute or electronic check was altered or had a fraudulent signature, the presumption is that the check was altered. BOFDs are denying claims of alteration on these types of checks without making the original paper check available for inspection, as the regulation demands. They continue to deny claims even after being presented with the regulation itself. Paying banks have no available options to fight these denials, which are clearly outlined in the current law, without pursuing legal representation. The cost of such representation will most likely lead to additional monetary losses to the paying bank. Community banks lack the financial resources to engage in prolonged legal battles against large national banks that leverage vast resources to evade accountability for fraud.
- 4) Priority must be placed on ensuring large national financial institutions exercise rigorous customer due diligence at the time of account opening, especially in non-face-to-face scenarios. A lax approach in today’s digital banking environment has proven costly to smaller community banks.
- 5) Due to the source of most check fraud beginning at large, national banks, it should be required that these large banks have their fraud department contact information for other financial institutions to use listed on their website or a national database be developed for providing this information.
- 6) There is a need for good, legal resources that community banks can go to and ask questions about handling check fraud cases (as well as other payment fraud). State banking organizations always advise banks to “consult with your legal department” as their organization doesn’t want to be held liable. A directory of law offices or attorneys that

specialize in bank fraud when checks, ACH, Wires, P2P, RTP or FedNow is used to commit a crime is becoming necessary for banks to defend themselves.

- 7) Financial institutions face a significant compliance burden when required to report fraudulent activity based solely on limited details; often just the name of the BOFD and a potentially fictitious payee. Financial institutions face steep penalties for non-compliance, so they are incentivized to file a Suspicious Activity Report (SARs) even if the details are minimal, just to stay on the safe side. As staffing, training, and investigative demands increase, they consume valuable resources that would otherwise be dedicated to serving our customers.

Respectfully submitted FreedomBank, Elkader Iowa

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