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Viewpoint: Remote Checks Pose High Risk

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With the technology that exists today, there is no practical reason for continuing the use of remotely created checks. In fact, advanced technology makes them more dangerous than ever before. With the advent of new banking products such as remote deposit capture, those individuals attempting to commit fraud can submit unsigned checks without even paying a visit to a branch to deposit them. The remote submission of unsigned checks increases the velocity of items that can be submitted.

Remotely created checks create a significant risk to consumers and weaken the safety and integrity of the nation's payments systems. The banking industry should begin the process of discontinuing remotely created checks as quickly as possible.

A remotely created check or demand draft is an unsigned paper instrument used to debit the payer's bank account with or without specific authorization. Any organization or individual can create a remotely created check. All that is required for its use is the bank routing number, the individual or company's account number to be debited and a statement that the signature or authorization for the debit is on file.

Since it is a paper instrument without a signature, the risk is masked by the billions of signed checks flowing through the check clearing system. It's easy to see why the fraudulent use of this payment instrument is high and growing.

Any debit-payment instrument — including automated clearing house items — is inherently risky, or at least riskier than using an ACH credit such as direct deposit or a credit card. A recurring ACH debit such as a utility bill payment, a mortgage loan payment or an insurance payment between known parties has the lowest risk. The primary reason for using ACH for these types of payments is the lower cost and efficiency of not using a paper document.

The risk rises exponentially for ad hoc or spontaneous debits, whether they are ACH or remotely created checks. Using these instruments for Internet or telephone purchases of products and services is extremely risky to the originators and receivers of these payments. The best payment instrument for these transactions is the credit card, because of the extensive risk-mitigation procedures and the sophisticated chargeback systems that have been developed for spontaneous payments.

By contrast, the ACH and paper-check systems were never designed for this purpose. If an individual was cheated by a telemarketer or a merchant with a defective product, there is no way for the consumer to charge back the transaction other than to claim that it is unauthorized.

So if the risk is basically the same, why is ACH better than remotely created checks? The answer is simple: One is electronic and the other is paper based.

The electronic debit by its nature can be tracked easily when it is returned. Nacha, the organization that sets the rules for ACH transactions, has exact national statistics supplied by the two ACH operators on how many debits were returned by transaction type and individual reason code (e.g., insufficient funds, account closed, invalid account and unauthorized).

The paper process makes tracking remotely created checks impossible, because there is no practical way to know the number of forward remotely created checks or the number of returns. There are no available statistics on the return rates for remotely created checks, because they cannot be automated, and the returns are bundled with the returns of all checks. As a result, the total number of remotely created checks returned as unauthorized or fraudulent is unknown.

By comparison, abuses by originators of ACH debits can be spotted very quickly, usually within a day, because the ACH operators have automated monitoring tools that can identify, by originator and originating bank, any company that has an unacceptable unauthorized return rate.

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