

FEDERAL RESERVE CHECK SERVICES

CONTAMINATED CHECK PROCEDURES FOR DEPOSITORY FINANCIAL INSTITUTIONS (DFIs) IMPACTED BY HURRICANE KATRINA

Hurricane Katrina and the subsequent flooding that occurred in many areas of Louisiana and the Gulf Coast created the potential for Depository Institutions to be in the possession of contaminated checks. This situation may have occurred with checks deposited in ATMs or items that could not be protected from the environment in banks, branches, operations centers and retail customers. Contaminated checks are those that may have been subjected to floodwater or prolonged exposure to water or other liquids. As a result of exposure, they may have come into contact with sewage, chemicals, or human matter that makes the items unsuitable for handling and personal contact. Contaminated checks could create health issues for any party involved in the collection process. The Federal Reserve Banks would like to offer DFIs guidelines to assist the industry in collecting contaminated checks and minimizing the potential for health issues.

To minimize subsequent handling of contaminated checks passing through the collection stream because of health issues cited previously, the Federal Reserve Banks strongly recommend all DFIs consider one of the following alternatives for collection of contaminated items:

CONTAMINATED CHECK COLLECTION PROCEDURES USING ACH

- ACH rules allow destroyed checks to be created and collected using the Automated Clearinghouse system under the Destroyed Check Entry (XCK) format. This collection alternative can be utilized for forward items only. Most ACH origination software supports the destroyed check format. Refer to the NACHA ACH Rules Book, pages OG 159 - 161 for details. There are several restrictions listed; such as a check must be less than \$2,500. However, due to the extenuating circumstances, NACHA's ACH Rules Enforcement Panel decided retroactive Thursday, September 1, 2005; they would not impose penalties on financial institutions when compliance with the XCK restrictions is not practical. This waiver will continue until October 31, 2005. In addition, the Treasury has agreed to accept U.S. Treasury Checks under the XCK format. However, Postal Money Orders cannot be collected using XCK and must be submitted using the check photo in lieu procedures described below. ODFIs should be aware the acceptance of XCK entries is optional although NACHA will be encouraging RDFIs to be accommodative due to the extenuating circumstances. Additionally, the ACH XCK format has a two character discretionary field in the entry detail record where you could identify the entries as Hurricane Katrina (HK). You should contact your ACH software vendor if there are questions regarding this format.

CONTAMINATED CHECK COLLECTION PROCEDURES USING CHECK CHANNELS

- If the items have been processed and filmed prior to contamination, an indemnified film copy in lieu of the original should be submitted.

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- If the items had not been processed, consider the use of a recodak film machine to create a collectible film copy in lieu of the original.
- If readily available, use of a copy machine to create a legible photo in lieu of the original.
- If you or an affiliate has Check 21 software, convert the item into a Check 21 item for electronic collection.
- If none of the above alternatives are available, contact the paying bank and request instruction on direct presentment and collection.

A properly prepared photocopy is defined in section 22.4 (d) of Operating Circular 3: "A correctly prepared photocopy must be a legible copy of the front and back of the cash item and must bear the sender's current indorsement and the following or equivalent signed legend: 'This is a photocopy of the original check which we indorsed and which was reported missing or destroyed in the regular course of bank collection. We guarantee all prior and any missing indorsements and the validity of this copy. Upon payment of this copy, we agree to hold each collecting bank and the payor bank harmless from any loss suffered, if payment is stopped on the original check and the original check remains unpaid.'" Photos in lieu should be placed in carrier documents, encoded and submitted for collection with other check deposits. Questions related to the proper deposit may be directed to the Adjustments area.

As with normal check deposits, contaminated checks must be readable with the dollar amount, paying bank identification and payee information clearly legible on the check. If this information is not available, you should consider requesting that the customer obtain a replacement check.

It is anticipated that most DFIs would have access to recodak or copying equipment either locally or through a partner institution to allow collection via photocopy. If you or your third party processor do not have access to ACH origination software with the XCK format, we may be able to assist you in locating either a vendor or another third party with these origination capabilities. If you need our help in facilitating a solution, please contact the Federal Reserve Banks' FedACH Customer Support Center at 1-866-234-5681.