



# PRESIDIO

## Business Check Fraud Prevention

### *Fighting Check Fraud Today*

Provides information regarding types of Check Fraud, how to combat check fraud, forgery, and counterfeit checks, tips on how you can prevent check fraud.

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#### What is Check Fraud?

Check fraud is one of the largest challenges facing businesses and financial institutions today. With the advancement of computer technology it increasingly easy for criminals, either independently or in organized gangs, to manipulate checks in such a way as to deceive innocent victims expecting value in exchange for their money.

A significant amount of check fraud is due to counterfeiting through desktop publishing and copying to create or duplicate an actual financial document, as well as chemical alteration, which consists of removing some or all of the information and manipulating it to the benefit of the criminal. Victims include financial institutions, businesses who accept and issue checks, and the consumer. In most cases, these crimes begin with the theft of a financial document. It can be perpetrated as easily as someone stealing a blank check from your home or vehicle during a burglary, searching for a canceled or old check in the garbage, or removing a check you have mailed to pay a bill from the mailbox.

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#### Types of Check Fraud:

##### Forgery

For a business, forgery typically takes place when an employee issues a check without proper authorization. Criminals will also steal a check, endorse it and present for payment at a retail location or at the bank teller window, using bogus personal identification.

##### Counterfeiting and Alteration

- Counterfeiting can either mean wholly fabricating a check --using readily available desktop publishing equipment consisting of a personal computer, scanner, sophisticated software and high-grade laser printer -- or simply duplicating a check with advanced color photocopiers.
- Alteration primarily refers to using chemicals and solvents such as acetone, brake fluid

and bleach to remove or modify handwriting and information on the check. When performed on specific locations on the check such as the payee's name or amount, it is called-spot alteration; When an attempt to erase information from the entire check is made, it is called-check washing.

### **Paperhanging**

This problem primarily has to do with people purposely writing checks on closed accounts (their own or others), as well as reordering checks on closed accounts (their own or others).

### **Check Kiting**

Check Kiting is opening accounts at two or more institutions and using "the float time" of available funds to create fraudulent balances. This fraud has become easier in recent years due to new regulations requiring banks to make funds available sooner, combined with increasingly competitive banking practices.

It has been estimated that the annual losses due to check fraud are in the billions of dollars and continue to grow steadily as criminals continue to seek ways to earn a living by defrauding others.

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### **Signs for bad checks:**

Below are several signs which may indicate a bad check. While one sign on its own does not guarantee a check to be counterfeit, the greater the number of signs, the greater the possibility that the check is bad.

1. The check lacks perforations.
2. The check number is either missing or does not change.
3. The check number is low (like 101 up to 400) on personal checks or (like 1001 up to 1500) on business checks. (90% of bad checks are written on accounts less than one year old.)
4. The type of font used to print the customer's name looks visibly different from the font used to print the address.
5. Additions to the check (i.e. phone numbers) have been written by hand.
6. The customer's address is missing.
7. The address of the bank is missing.
8. There are stains or discolorations on the check possibly caused by erasures or

alterations.

9. The numbers printed along the bottoms of the check (called Magnetic Ink Character Recognition, or MICR, coding) is shiny. Real magnetic ink is dull and non glossy in appearance.
10. The MICR encoding at the bottom of the check does not match the check number.
11. The MICR numbers are missing.
12. The MICR coding does not match the bank district and the routing symbol in the upper right-hand corner of the check.
13. The name of the payee appears to have been printed by a typewriter. Most payroll, expenses, and dividend checks are printed via computer.
14. The word VOID appears across the check.
15. Notations appear in the memo section listing "load," "payroll," or "dividends." Most legitimate companies have separate accounts for these functions, eliminating a need for such notations.
16. The check lacks an authorized signature.

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## **Check Fraud Tips for Businesses**

### **Businesses as Check Fraud Victims**

It is widely believed that businesses are the primary targets of check fraud professionals - especially by organized rings of criminals. As far as counterfeiting and alteration, payroll checks appear to be a favorite although all forms of business checks are targets from time to time and all forms of fraud techniques are practiced as well.

### **Uniform Commercial Code - Who is responsible?**

It is clear now that businesses must play a role in ensuring their checks are secure. Recently revised UCC regulations add the onus of shared responsibility for check fraud on the business. For example, if a bank offers their customer check stock that contains security features that could have prevented a specific case of fraud, the bank can claim that the customer was negligent and therefore at least partially liable for the fraud loss.

### **Check Fraud Tips**

A combination of precautions that a business might undertake could greatly reduce the likelihood of check fraud. Poor internal controls may lead to collusion between employees or

third parties who copy, steal, alter and forge checks.

### **Order checks and deposit slips wisely**

- Use an established, respectable source, especially those recommended by your bank, to ensure your checks will process easily through the bank's clearing system.
- Make sure that your checks include Security Features that will help combat counterfeiting and alteration.
- Make sure you notify your check supplier (and financial institution, if necessary) if a new check order has not been received within a reasonable amount of time after you ordered them.

### **Maintain adequate physical security of your checks, deposit slips, etc.**

- Secure all reserve supplies of checks, deposit slips and other banking documents in a locked facility. Keep blank checks locked up at all times and limit the number of people with access to your checks. If your checks fall into the possession of unscrupulous employees, you could be liable for substantial losses.
- Change the locks on your facility when an employee leaves your employ.
- Never leave checks or bank records unattended in order to assist customers.

### **Issuing and reconciling checks**

- Assign accounts payable functions to more than one person and make each one responsible for different payment areas. This division of responsibility makes it more difficult for employees to tamper with checks and payments.
- Limit the number of official signers. The fewer check signers you have, the lower your chances are of being defrauded.
- Require more than one signature on large dollar check amounts. In this way, any losses you may incur will be low denominations only.
- Immediately notify the bank of any change to your accounts payable process and personnel. You don't want former employees who may have secreted some checks from your business to retain authorization to sign them after they have left your employ.
- Separate the check writing and account reconciliation functions. Try not to have the same person who balanced the bank statement issue checks. This provides greater safeguards against an employee writing fraudulent checks and covering it up. The reconciler would be able to prevent the crime unless the employees are in collusion.
- Reconcile your account promptly and regularly -- quick fraud detection increases the likelihood of recovery. Businesses and personal consumers who do not balance their

accounts monthly and don't find the discrepancies until months have passed, can become liable for losses.

### **Fraud Prevention Services (provided by the bank)**

- **Use Positive Pay.** This type of payment system records pertinent information about each check such as the amount, the check number, bank information and date, and then transmits it to the bank to be verified, before the check can be paid.

### **Employee relations policies**

- **Make sure you know who you are hiring to handle your money.** Diligent reference and background investigations on all prospective employees are important so you know that you are not hiring someone with a past record of financial abuse.
- **Conduct random audits and enforce vacation policies.**
- **Have your employees bonded.**

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### **Tips For Detecting Counterfeit Checks:**

1. **COLOR** - By fanning through a group of returned checks, a counterfeit may stand out as having a slightly different color than the rest of the checks in the batch.
2. **PERFORATION** - Most checks produced by a legitimate printer are perforated and have at least one rough edge. However, many companies are now using in-house laser printers with MICR capabilities to generate their own checks from blank stock. These checks may have a micro-perforated edge that is difficult to detect.
3. **MICR LINE INK** - Most, but not all, forgers lack the ability to encode with magnetic ink the bank and customer account information on the bottom of a check. They will often substitute regular toner or ink for magnetic ink, which is dull and non-reflective. Real magnetic ink applied by laser printers is the exception and may have a shine or gloss.

If a counterfeits MICR line is printed or altered with non-magnetic ink, the banks sorting equipment will be unable to read the MICR line, thus causing a reject item. Unfortunately, the bank will normally apply a new magnetic strip and process the check. This works to the forgers advantage because it takes additional time to process the fraudulent check, reducing the time the bank has to return the item. But banks cannot treat every non-MICR check as a fraudulent item because millions of legitimate checks are rejected each day due to unreadable MICR lines.

4. **ROUTING NUMBERS** - The nine-digit number between the colon brackets on the bottom of a check is the routing number of the bank on which the check is drawn. The first two digits indicate in which of the 12 Federal Reserve Districts the bank is located. It is important that these digits be compared to the location of the bank because a forger will sometimes

**change the routing number on the check to an incorrect Federal Reserve Bank to buy more time.**

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