



What is Check 21?

CHECK 21

- » The “Check Clearing for the 21st Century Act”, also known as “Check 21”, is a federal law that was enacted to create a more efficient and secure means for the processing and clearing of checks.
- » Prior to its inception on October 28, 2004, the check processing system relied on physically transporting paper checks from one location to the next.
- » Check 21 encourages check truncation (the replacement of a paper check with a digital image) by removing the need to physically transport a check between banks. This decreases the processing times and transportation costs, while reducing the likelihood of items being lost or destroyed in transit.

» What Is a Substitute Check?

Because of Check 21, the bank of first deposit can now transfer a digital image of the check to the check processor and ultimately to the paying bank. If the paying bank is not fully image enabled, or is not able to process an electronic version of the check it can receive a paper version of the check called a substitute check (or image replacement document—“IRD”). An IRD is a paper replacement check created from the electronic image of an original paper check, and is the legal equivalent of the original check.

Because the IRD is a legal version of the original check, the financial institution has the option of either storing or destroying the original document once it has been captured electronically.

According to Check 21 guidelines, the substitute check must contain all of the information on both the front and back of the check, including the MICR line and all endorsements, and also states that it is a legal copy of the original check.

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This is an example of an IRD



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What is Check 21? (continued)

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» Why Would a Bank Choose to Print IRDs?

There are many reasons why a bank may chose to print IRDs. Because IRDs replace a physical check, they practically eliminate courier and transportation fees associated with sending a hard copy of a check. These cost savings can add up for large institutions.

Another benefit to eliminating the physical transportation of checks is the reduction in the amount of float. Since the files are transmitted electronically banks are able to process them much quicker than through traditional means.

Perhaps one of the largest motivations for banks to print IRDs is the ability to expand their customer base. Check 21 has created many opportunities for banks to leverage the technology for other purposes. The same technology can be used for merchant customers who deposit checks on a regular basis. Since the files can now be transmitted electronically banks no longer need to have a brick and mortar branch in proximity to their merchant customers. This creates an opportunity for banks to greatly expand their customer base and to create relationships with new merchant customers that wouldn't have been possible in the past.

Check imaging and the printing of IRDs create many other opportunities for banks to cut costs, expand their customer base and streamline their operations.

Helpful Terms:

What do all the terms mean that are associated with Check 21 and IRDs?

Cash Letter

A "letter" that accompanies a bundle of paper checks sent from one financial institution to another, describes what's in the bundle (# of items, \$ amounts, etc.)

Electronic Cash Letter (ECL)

Provides cash letter information PLUS the check images and data in electronic formats called X9.37 and X9.100-180 files

Bank of 1st Deposit (BOFD)

The bank where the check is deposited

Intermediary (Federal Reserve or large bank)

An intermediate recipient of checks for processing

Correspondent Bank

Provides services to other banks, including check processing services and IRD printing

Payor Bank

The bank that the check is drawn on (opposite of BOFD)

Forward Items (AKA "Day One")

Checks on their way to the payor bank

Return Items (AKA "Day Two")

Checks on their way back to the BOFD because of insufficient funds, unreadable check, or other reason

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