21st March 2014

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Cheque Imaging Consultation
Banking & Credit Team
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Dear Sirs,

**C&CCC RESPONSE TO HMT CONSULTATION PUBLISHED 6TH MARCH 2014 "SPEEDING UP CHEQUE PAYMENTS: LEGISLATING FOR CHEQUE IMAGING''**

The Cheque and Credit Clearing Company (C&CCC) is a membership-based industry body which manages the cheque clearing system in Great Britain. The Company was established in 1985 and from that time until the present day it is proud of its record in:

- providing consumers, via Financial Institutions, with the central payment system services for the exchange and settlement of cheques and credits. These services are underpinned by payments infrastructure including exchange centres, the network for the transfer of electronic cheque data, and an automated settlement system. It also includes a courier service for the return of unpaid cheques to the collecting bank;
- managing the operational processes of the central payment system services;
- determining the rules, standards, and procedures required to maintain the integrity of the clearings, including the criteria for joining the clearings and ensuring compliance with those rules;
- engaging with the full range of stakeholders, which includes consumers and businesses that use cheques, banks that offer cheque clearing services, cheque processors, cheque printers and other suppliers, as well as regulators, trade associations and other payment schemes.

A Company incorporated in England No 1962903.
Registered Office as opposite

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**Objectives**

The overall objectives of the Company are to:-

- maintain the integrity and sustainability of the clearings which have been operating in a declining market for some time,
- respond proactively to changes in the business and regulatory environments;
- facilitate innovation in the clearing process in order to deliver improvement in the customer proposition and, equally important, improvements in industry efficiency,
- maintain a trusted centre of excellence, experience and expertise in the cheque and credit clearings.

In December 2013, the C&CCC Board reached an important milestone decision to adopt, as its strategy, a new Future Clearing Model which would deliver its overall objectives, as above, utilising an image based processing system, replacing the current, largely paper based processing approach.

As part of this strategy, the C&CCC Board agreed that there should be one single UK Sterling cheque and credit clearing scheme, offering the potential for a shorter clearing cycle and providing a variety of choices for those customers who have made it quite plain that they wish to continue to pay-in or issue cheques.

The image based Future Clearing Model would enable the Company to offer direct and indirect participation for processing access to the scheme in addition to direct and indirect settlement membership options. The central, image based clearing will be based on the exchange of data and images (front and back) and not paper with the Paying bank (be it a C&CCC Member or an agency bank participant) having the ability to readily obtain images of all items drawn on them.

Two key priorities in the development of a new image based cheque and credit processing model are to ensure that the opportunity for fraud does not increase (and if possible is decreased) and that settlement risk is reduced and, if possible, eliminated.

We see the new image based clearing model providing improved sustainability for cheques, thereby enabling further innovation to take account of technological developments as they occur, and addressing customer requirements so that the cheque will continue to be available for their use for as long as the demand is present.

In order to support your consultation we would make the following comments in respect of the questions you have asked:

**Question 1**

*The current cheque system faces a number of challenges, and legislation to introduce cheque imaging will help resolve these and deliver a set of wider benefits, as set out above. Do you agree with this analysis?*

We agree that cheque imaging will help to deliver a wide set of benefits and is only achievable with specific legislative changes.

Customers have made it very clear that they want to be able to use cheques as part of the range of **payment choices** they have. While cheque usage has declined steadily over the past 20 years, a sizeable number of cheque users remain and they want to be sure that they can carry on using cheques for as long as they want to. The Company fully understands and supports this requirement and believes that by moving to an image based clearing process we would secure **process efficiencies** which would enable us to sustain economically viable services, whether demand continues to decrease, plateau or whether, for any reason, it should increase.

By removing the costly and time consuming requirement to move cheque paper by road, and in some cases by air, from collecting branch to out-clearing centre, then onwards to the exchange centre and finally to in-clearing centres, cheque imaging makes it possible to **improve on the current clearing cycle**. Whereas there is as yet no clear evidence to support a view that speeding up the clearing cycle is a key customer requirement, it is nonetheless often quoted generally that people feel that cheque clearing is too slow. Many consumers remain confused about when they can access funds, despite our promotion of the 2-4-6 campaign, and shorter clearing cycles may help improve clarity and understanding. We believe that the only way clearing can be speeded up is to remove completely the statutory right and reliance, by paying banks, on receiving original cheque paper via the clearing before making their decision to pay, or not pay, the cheque. Cheque imaging means that the original cheque paper can be truncated at the point of first deposit, with only the digital image (front and back) of the cheque being used for all processing thereafter.

Cheque imaging also offers the opportunity to respond readily to **further technological advances** which, if we were to remain tied to paper based processing, would be very difficult.

The Company welcomes the opportunities for **reducing barriers to entry** so that challenger banks which want to participate directly in the cheque clearing can do so more easily than they do now, even if they do not have a branch network. It is important that imaging is introduced in ways that enhance, rather than restrict, consumer choice.

Recent publicity surrounding the move to cheque imaging centred on the ability of customers receiving a cheque to send an image of the cheque to their branch to be paid in to their account. This **innovation and enhanced customer proposition** is a clear benefit for those who use smartphones, but it is important to note that cheque imaging is not reliant on smart phones and that many of the process efficiencies and enhanced sustainability can be achieved in the 'back office', without imposing any new requirements on customers, particularly the digitally and socially excluded. Customers receiving cheques will be able to pay them in exactly as they do now but choice will be extended as some banks may offer, in addition to the base service, further enhancements which use smart phone technology to pay cheques in, if that is their preference, thus removing the requirement to go to a branch.

In addition to smartphone technology other image technology could also be offered to customers. For example, some banks may offer business payees the ability to deposit cheques by scanning their images, thereby automating the cheque collection process still further. In the US this is known as Remote Deposit Capture, where a scanning device, capturing cheque images and code line data, is offered to corporate and business customers enabling them to process their own items via their online banking arrangements.

*Specifically, we are interested in views and evidence on the following points:*

- *the costs (quantifiable or non-quantifiable) of the current system*
- *the benefits (quantifiable or non-quantifiable) of introducing cheque imaging*
- *the costs (quantifiable or non-quantifiable) of introducing cheque imaging*
- *the appetite (among both payment service providers and customers) for adopting smartphone technology for the paying in of cheques*
- *the experience of other countries in introducing cheque imaging*

There is no record centrally of the costs of the current system (part of which is executed in-house by the banks, and part via competing third party service providers) due to competition law constraints. Within the Future Clearing Model, the costs will depend on how individual banks choose to implement the new system.

The benefits of introducing an image based cheque processing system include:-

- increased longevity of cheques for customers who wish to use them
- potential for delivery of a faster clearing cycle
- new image based products and bank channels would be available for customers, e.g. remote deposit capture
- enabling banks to offer smart phone apps so that their customers can pay in via image
- the housebound and others who find it difficult to visit branches would find it easier and more secure to pay in cheques
- customer to receive faster notification of unpaid cheques
- enable cheque issuing customers to have the ability to receive or access images of paid items for their records,
- customers could have the ability to pay cheques into UK bank accounts from anywhere in the world
- more competition with regional Financial Institutions able to compete nationally
- accommodation of the cheque redirection service as part of the overall account switching service
- common UK proposition irrespective of weather, flights, fuel shortages etc;
- more competition on unique selling points between banks
- Agency Banks able to move readily between different settlement banks and infrastructure providers
- more competition between payment systems - C&CCC would be able to compete with electronic schemes (i.e. Bacs Direct Credits) on clearing timescales and potentially other new services
- more competition for the tender of the central switch for image exchange, thereby providing competition with incumbent suppliers to other schemes.
- more electronic handling enabling easier reconciliation
- changing the cost model, enabling costs to be taken out of fixed costs rather than just concentrating on ongoing reductions in variable costs with the potential for ‘plug and play’ facilities giving parity costs for all
- guaranteed capped prefunded settlement which removes settlement risk and enhances payment system financial stability
- removing the current constraints of paper processing on the lead pair sort codes, to enable sort code flexibility in line with the electronic schemes.
- enabling Financial Institutions the choice of where images can be captured, for example at their branches or at processing centres
- using images in place of paper in the unpaid process and removal of the need for dedicated courier runs to transport paper
- image enabled fraud detection taking advantage of improved fraud detection technology
- reduced timeframe for new entrants to join the market offering clearing facilities.

From our Stakeholder Forums feedback we believe that there is appetite from some receivers of cheques to have a smart phone app as an extra option which they could use to pay in cheques conveniently. Our current market research is published on our website, along with the feedback from our last Cheque User Forum at www.chequeandcredit.co.uk. The Company is planning to undertake further market research including focus groups to assess customers' wishes as our Future Clearing Model develops.

The Company would want to enable and support Financial Institutions to compete and innovate customer propositions in this area, based on their own views of the market demand for the use of smart phone technology.

**Our focus is on enabling customer choice**. In enabling the scheme to accept the use of smart phone technology by our Members and Agency Banks, those customers who want to use it (and any other technology that may emerge in the future) can do so without constraining their ability to continue to use cheques as they do today, i.e. without it being necessary or mandatory for customers to use such technology.

We are aware that a number of other countries around the world in addition to the US all use cheque imaging models e.g Malaysia, China, India, New Zealand, Australia, Hong Kong, Singapore, Mexico, Chile, Brazil, Israel and France. A large amount of information is available in the public domain on each of these, for example the US FED quotes '*that by shifting to electronic collection and presentment, the Federal Reserve reduced its per item cheque processing cost by **over 70%****. It is only in the US that we are aware of any specific cost information.

**Source: 'Getting Rid of Paper: Savings from Check 21' David B Humphrey, Florida State University, Tallahassee, FL, U.S.A. Robert Hunt, Federal Reserve Bank of Philadelphia, Philadelphia, PA, U.S.A. May, 2012

**Question 2**

*The current legislation preserves the practice of exchanging paper instruments, and does not accommodate the transmission of digital images. Do you agree that the legislation should be amended to remove the right of the paying bank to demand delivery of the original paper cheque, and require a certified, digital image of the cheque to be treated as equivalent to the original paper cheque for the purposes of presentment?*

**We believe that it is essential for legislation to be amended as described**.

The Company has received legal advice, supported by senior counsel, that the current legislation (Bills of Exchange Act 1882; Cheques Act 1957; Deregulation Bills Order 1996) requires amendment to deal with four broad points:-

- It is essential that an **image** of the cheque **should be treated as equivalent to** the original **paper** cheque for the purposes of presentment, thus removing the right of the paying bank to call for physical paper, at any time after completion of the clearing process, as it undermines the practical efficiency of the image model. The image model relies in total on the cheque image for all processing following image capture. It would be impractical to be required to set up systems for the search and retrieval of some paper, if and when called for by the paying bank. The ability of the paying bank to demand that paper be delivered is one of the reasons why the paper clearing has continued in its current form and if this ability is not removed it will negate the beneficial effect of this legislation. For example, customers using a smart phone app would not want to still have to pay in the original paper cheque given that the benefit of the smartphone app is to pay in via image only.
- The existing truncation legislation, which enables cheques to be truncated at the collecting bank, refers to cheques only and not to other items processed in the clearing (e.g **travellers cheques, warrants, payable orders**, etc). If we were to rely on existing truncation legislation, it would be necessary for the Company to set up a separate, paper based, operation for items such as payable orders, warrants and travellers cheques. Although these items are not high in volume they are currently processed seamlessly in the clearing alongside cheques and we feel that it is in the interests of efficiency and good customer service to have one image based clearing for all items presented in the clearing. This requires a change to truncation legislation to effectively include all items processed in the cheque clearing within the new customer proposition.

- The existing truncation legislation requires the **essential features** of the cheque (defined as the codeline) to be transmitted from collecting bank to paying bank whereas, under the image model, the full image, front and back, of the cheque would be transmitted. This may seem a small change but we require the full image to be transmitted in order to facilitate fraud and technical checks (signature, date, payee name) at the paying bank and to serve as the only record of the original cheque to be returned to the collecting bank in the event of non-payment, e.g. through lack of funds, and to provide evidence of payment should it be required in a court of law. The 'essential features' and the codeline detail would not be sufficient for these purposes.
- Should the ability to demand paper persist, collecting banks would continue to deliver all paper collected rather than identify and out sort only those paper items that the Paying bank requires, as the former is easier and less time consuming than differentiating. Removing the **right to require presentment** of paper cheques is an essential prerequisite to make the systemic shift to image.

**Question 3**

*Do you agree that the government should legislate to protect the choice of customers to deposit paper cheques in branch, even where there is the option of paying in via smartphone?*

Yes. We would support such legislation since it **promotes choice while encouraging innovation**. The ability to offer a new service, where customers can scan in cheques using their smartphone, via ATMs or other means, will enable banks to compete on customer proposition and could enhance the position of challenger banks without an extensive branch network.

However, at the same time we believe it is vital that customers continue to be able to deposit cheques in paper form at a branch counter if they so wish, so that they do not need to change their behaviour at all. This will be particularly important for the digitally, financially and socially excluded personal customer for whom cheques are a particularly important payment system. For these customers the main benefit of a move to image based processing is the economic efficiencies to be gained, increasing the long term sustainability of the cheque clearing system and hence its availability as an option within an array of electronically based payment systems. The key message is that payee imaging is an additional facility and not a replacement one.

**Question 4**

*The government believes there is a strong case for the industry moving as one onto a cheque imaging model with a central scheme infrastructure, but is willing to consider permitting banks to request paper substitute cheques as an alternative.*
*Should the government legislate for a date by which all Financial Institutions must be ready to accept cheque images? If so, what is a reasonable period of time to allow the industry to prepare for cheque imaging?*

We are currently working hard with our Members to get to a point by our Board meeting on the 1st May 2014 where we will have a much better idea of the scope of the programme which will enable us to better estimate the length of time we will need to safely implement a new image based cheque clearing. Given that the changes being proposed have to be made to live processes, and that they will require extensive testing prior to implementation, we must ensure that we allow sufficient time to implement so that we do not introduce risk to the integrity of the cheque clearing.

We believe that Financial Institutions should move to an image based processing system together, as an industry, in order to protect the integrity of the clearing. Therefore, we believe that the government should legislate for a time by which all Financial Institutions must be ready to accept cheque images. Moving together would bring about benefits of a common processing platform and common service standard whereas, if Financial Institutions move at different times, there would be reduced ability to control standards and common approaches to consumer protection, which would in turn be confusing for the end user.

Our experience of major programme deliveries such as this is that they require in the region of 2 to 4 years from inception to implementation and this is currently the only guide we have as to the likely time in would take to allow the industry to prepare for cheque imaging . However, in order to maintain the integrity of the clearing it is critical that the time required for making radical changes to live payments processing operations is based on the need to ensure that the new systems are fully tested end to end and that they are fit for purpose and robust before full implementation. The work we are currently doing to design and agree a specification for our Future Clearing Model will enable us to give a better idea of how we would introduce an image based solution in the UK, at which point we would be in a better position to determine, more precisely, the time required to build it.

We are aware that there are resource issues for Financial Institutions, both in terms of our Member Banks and our Agency Banks, in prioritising the work involved on their side to implement the core industry enablers for cheque imaging which will impact the delivery timescales.

*Or should the legislation provide the option for Financial Institutions to accept an Image Replacement Document (IRD) as an alternative?*

No.  Image Replacement Documents (IRDs) were used **in the US** as part of their Check21 programme but it should be noted that one of the key differences between cheques in the US and UK is that in the UK the cheque paper itself contains many security features (e.g the ink, the paper itself, holograms) which are not present on US cheques. In the US, therefore, it was felt that by producing a paper copy of the cheque image, the IRD, it would provide a degree of comfort to a paying bank wishing to view or hold a physical copy of the original cheque.  In fact, **the IRD proved to be unnecessary** as banks and customers were happy to rely on the digital image alone and the use of the IRD in the US has now practically ceased.

**In the UK**, provided the current legislation is changed so that the image of the cheque is acceptable in all cases in place of the original cheque, there would be **no advantage in introducing an IRD**.  The IRD is not an acceptable or practical alternative to the current paper based system or to image and its use could be seen as cheque dematerialisation and not truncation**.** We understand that such dematerialisation would be more difficult to achieve through legislation than image truncation.

*A new model of "1-2-2" has been put forward as a desirable and realistic target for the industry. Do you agree?*

There is a very real **opportunity for shortening the clearing cycle** under an image based processing system which is simply not possible with a paper based clearing. We believe that a T+1-2-2 clearing cycle is achievable provided the systems in place are robust in order to ensure no fraud or settlement risk is introduced as a result.  However, it may be that customers are more concerned about greater certainty and clarity of when funds become available to the recipient to regard as their own, i.e to spend.
We note that the current T+2-4-6 model is hard for customers to understand and we would prefer any new clearing cycle to be much simpler for the benefit of customers.

**Question 5**
*Do you agree that the proposed legislative changes should apply to all of these paper instruments, to allow them to be cleared in image form?*

Yes. The existing truncation legislation, which enables cheques to be truncated at the collecting bank, refers to cheques only whereas items other than cheques are processed in the clearing (e.g **travellers' cheques, warrants, payable orders**, etc). If we were to rely on existing truncation legislation, it would be necessary for the Company to set up a separate, paper based operation for items such as payable orders, warrants and travellers cheques. Although these items are not high in volume they are currently processed seamlessly in the clearing alongside cheques and we feel that it is in the interests of efficiency and good customer service to have **one image based clearing** for all items presented in the clearing. This requires a change to truncation legislation to effectively include all items processed in the cheque clearing.

**Credits do not need to be included** in the revised legislation as they are not currently covered by statute. The Credit Clearing will continue and is included in the scope for the Future Clearing Model.

**Question 6**
*Do you agree that liability should be with the collecting bank, rather than the paying bank? For agency arrangements, should the liability be with the collecting bank, or the beneficiary bank, or shared between them? The government would particularly welcome comments from banks and building societies with agency relationships. Should the government impose specific due diligence obligations on the collecting and/or beneficiary bank, as well/instead of transferring the liability?*

**The liability, under existing law, rests with the collecting bank** so the introduction of an image based processing system has no impact on current liability. However, this is a complex area and current custom and practice by Financial Institutions has led to a perception that legal liability sits with the paying bank which recent external Queen's Counsel opinion for C&CCC has confirmed is not the case. As such, we believe that the opportunity should be taken to clarify where liability rests and it would be helpful to have this enshrined in law and cascaded throughout the company's governance documentation. We believe that this clarification is a key factor in gaining the small Agency Banks' approval for a move to image based processing as they think that if the current process continues (where the paying bank accepts liability for fraud) they will have to invest heavily in new technology. With the liability clarified, the collecting bank accepts liability for those matters over which it has control without the necessity of the paying bank proving negligence on behalf of the collecting bank. Such a clarification also brings liability more into line with that in the electronic schemes. It is important to stress that customers using cheques will never be liable for a cheque fraud loss, provided they were not a knowing party to that cheque fraud.

The liability for cheque and credit fraud should rest with the collecting bank (being the bank where the transaction is paid in over the branch counter) as this is the only point at which the full transaction set (the cheque and the credit) is present for examination. However, it is not always possible for the collecting bank to identify a well executed fraud. It should be remembered that the collecting bank is responsible for carrying out 'know your customer' (KYC) and anti money laundering (AML) checks so should ensure that their customer, who is presenting the cheque, is not fraudulent.

The important thing to note is that **the innocent customer must never foot the cost of fraud**. The industry is well aware of the risk of fraud relating to cheques and credits and has had some success in reducing fraud levels. We will continue to work together to reduce them further.

This area is further complicated by the fact that there are various types of cheque fraud that we are constantly working to mitigate and further information on each of these can be found on our website. www.chequeandcredit.co.uk. Whilst we have already briefed you on the detailed results of our external legal advice on cheque fraud liability we have also attached a summary in Appendix A.

**We would be happy to meet to discuss this response and would reiterate our willingness to work to achieve what we believe is an innovative and essential improvement to the current service. This advance will enable us to continue to deliver an excellent cheque clearing service for customers, suitable for the 21st century, which can be adapted for continued use for as long as it is required.**

Yours sincerely,

Angela Thomas
Cheque & Credit Clearing Company Ltd

**APPENDIX A**

*This information is a summary of the legal advice C&CCC has received and is a summary of the position of C&CCC. It has been provided for the benefit of C&CCC only and is published here for information. Whilst the information contained in the summary is correct at the time of issue, neither C&CCC nor its advisors accept any liability for its accuracy, adequacy or completeness, and nor is any express or implied warranty given. This exclusion extends to liability in relation to any statement, opinion or conclusion contained in or any omission from, the summary, but does not extend to any fraudulent misrepresentation made by or on behalf of C&CCC.*

*If a member or any third party wishes to use or rely on the information contained in the summary, such member or third party must seek its own legal advice.*

**REMOTE CAPTURE MODEL:**
**<u>SUMMARY OF ADVICE</u>**

## *A. Introduction*

1. This paper has been prepared at the request of C&CCC Scheme Governance Legal Sub-Group (the ***LSG***). It is intended to assist the LSG determine its recommendations to the C&CCC Board in respect of the proposed Remote Capture Model (the ***new model***); and, to that end, to facilitate consultation between members of the LSG and senior management at their respective institutions.

## *B. Background*

2. The new model is considered beneficial for three principal reasons.

   (1) It will move the clearing cycle to a "1-2-2" timescale. This would be a positive industry initiative in response to the challenge set by the Chancellor of the Exchequer, Rt Hon George Osborne MP, in his speech on the Reform of Banking given on 4 February 2013.

   (2) It will allow banks to introduce competitive service offerings to customers for instrument imaging/presentment. More broadly, it will reduce the administrative costs (and related operational risks) associated with the handling and delivery of physical instruments through the clearing.

   (3) It will enhance finality of inter-bank settlement, as well as the security and integrity of payments completed through the clearing.

3. The C&CCC has now received legal advice on the new model from Travers Smith LLP and Raymond Cox QC as to matters of English law; and from Dundas & Wilson CS LLP and Alistair Clark QC as to matters of Scots law.

## *C. Principal conclusions*

4. The legal advice has not identified any material legal obstacles to the introduction and implementation of the new model.

5. However, C&CCC has been advised that the new model will require certain changes to the legislative framework. These changes will:

   (1) support a ***full truncation model*** – under which an electronic image of the whole instrument will be sent to the paying bank by way of presentment of the instrument (and not just its "essential features" permitted under a partial truncation model) and

there will be a failure in due presentment if there is any material error in the image received by the paying bank;

(2) extend the benefits of full truncation not only to cheques, but also to bankers' drafts, postal orders, government payable orders, warrants and travellers' cheques (cheques and these other instruments being collectively ***relevant instruments*** which are currently cleared through the system);

(3) allow a customer who is a payee under a relevant instrument to perform certain functions under the new model (i.e. digital imaging and certification as a true copy) as agent for and under the responsibility of the collecting bank;

(4) remove the existing statutory right for the paying bank (under a partial truncation model) to require the collecting bank to present the physical instrument; and

(5) remove any impediments or restrictions in the statutory terms of issue for any relevant instrument which are inconsistent with the presentment of the instrument under the new model.

6. These statutory changes will need to be effected by way of *primary* legislation. Initial soundings of HM Treasury suggest that HM Government may be inclined to find suitable space in its legislative timetable for the changes required to support the new model.

***D. Supporting legal analysis***

7. In reaching these conclusions, the relevant legal issues were considered within three broad categories.

*(A) Rights and liabilities of the parties to a relevant instrument*

8. The new model should not adversely affect the rights and liabilities of the drawer/issuer or holder of a relevant instrument. In particular:

(1) the holder will be able to enforce payment of the relevant instrument against the drawer/issuer notwithstanding its destruction under the new model;

(2) a certified copy of the relevant instrument should be equivalent to the original instrument for evidential and receipt/voucher purposes – so that the drawer/issuer of a paid instrument (and its paying bank) should no longer require (and should no longer be entitled to) delivery up of the original instrument[1]; and

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[1] Scottish Counsel has, however, recommended that express statutory provision be made to exclude any residual common law right of the paying bank and/or the drawer/issuer to delivery up of the original paid instrument. This would support the legal certainty of the new model under Scottish law.

(3) the destruction of a relevant instrument will not result in its cancellation or renunciation by the payee and so will not discharge the drawer/issuer from liability on the instrument.

*(B) Rights and liabilities of the collecting bank and paying bank*

9. The new model should have no material impact on the rights and liabilities of a collecting bank and a paying bank in relation to a relevant instrument[2]. In particular:

(1) a collecting bank will act consistently with its contractual obligations to its customer (the payee) in effecting presentment of the relevant instrument under the new model;

(2) a paying bank will act consistently with its contractual obligations to its customer (the drawer/issuer) in making payment against presentment of the relevant instrument under the new model;

(3) although the liability for payment out on a forged or materially altered instrument will fall initially on the paying bank (for breach of mandate), under the new model (as today) the paying bank should be able to recover any mistaken payment from the collecting bank (subject to restitutionary defences);

(4) potential liability to the true owner (under English law) in conversion and (under Scots law) in negligence[3] will not be affected by the new model, and will remain subject to the statutory defences available to a paying bank and (in respect of conversion) to a collecting bank;

(5) the contractual responsibility of the paying bank will (as today) be to make its pay/no pay decision at the time of presentment (and there will, as today, be no duty on the paying bank to defer any decision on the basis that funds will or may come into the drawer's/issuer's account); and

(6) there is no material legal impediment to the proposed electronic "re-presentment" of a relevant instrument under the new model.

10. However, the new model will introduce two new *operational* sources of liability for banks. A paying bank may make payment against: (a) an erroneous or fraudulent second electronic

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[2] It will, however, be a matter for determination by HM Government as to whether from a policy perspective it would be appropriate to put in place a statutory "initiating bank liability" framework to enhance legal certainty and market confidence in the operation of the new model. This might impose strict liability (subject to limited statutory defences) on a collecting bank for its actions (or the actions of its agent) under the new model, where those actions result in loss to the paying bank and/or the drawer/issuer. It would create a private law action for breach of statutory duty against the collecting bank.

[3] Nor will the new model affect any potential claim to follow and trade the proceeds of a relevant instrument by its true owner.

presentment of the same instrument; or (b) against an image which (whether by reason of a fault in its electronic capture or in transmission) is not a true reproduction of the original instrument.

11. In both cases, a mistaken payment will have been made – in the first case, because the instrument will have been duly discharged on first presentment; and, in the second case, because a payment has been made against an instrument which has not been duly presented. Any such mistaken payment should, in the same way as a payment made against a forged or materially altered instrument, be recoverable by the paying bank from the collecting bank (subject to restitutionary defences).

12. Systems and controls will/can be expected to be put in place to minimise the risk of such double presentment/failure in due presentment under the new model. The C&CCC Board will need to weigh these new operational risks against the broader benefits of the new model.

*(C) No adverse interference with the day-to-day operation of the new model*

13. The efficient and effective operation of the new model should not be disrupted by actions or claims from third parties. In particular:

(1) the destruction of a relevant instrument under the new model should not itself give rise to liability to customers or the true owner – they will have given their express or implied consent to such destruction and/or they will suffer no loss by reason of such destruction;

(2) a court should not require the payee to provide an indemnity to the drawer/issuer as a condition to pursuing his action on a certified copy of a relevant instrument;

(3) a payee should have no right to require the drawer/issuer to provide a duplicate of an instrument destroyed under the new model; and

(4) no customer or the true owner should be able to obtain injunctive or similar relief from the courts to prevent the destruction of a relevant instrument under the new model.

*Mark Evans*
*Travers Smith LLP*
*20 September 2013*