Dual Signatures

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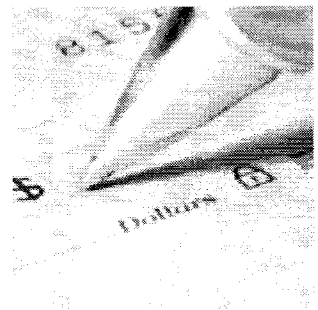
Are Dual Signatures a good internal control requirement?



Yes. An important internal control related to cash disbursements can include requiring two authorized signatures on all company checks generally over a specific amount that has been set by management or the board directors. By requiring two signatures, the company is verifying that both signers agree that the payment is proper and reasonable. The requirement of two signatures reduces the likelihood that one will write improper checks to themselves or writing checks to a fictitious company.

Are banks looking at your checks to verify that the dual signatures are on the checks?

No. Many companies are under the assumption that banks will be reviewing the checks and verifying that checks have two signatures, as required by the company. Banks are not looking for dual signatures–they process certain information from the check including verifying that there is an allowed signature but will not be looking past the first signature. Banks consider dual signatures to be an internal arrangement within the company between those authorized to sign checks and do not want the liability for verifying two signatures.

Should dual signatures still be required if the banks are not checking for dual signatures?

Yes. Continue to require dual signatures but know that it is your responsibility to verify that the internal control steps you have in place are working. There are several ways do this: the person who mails the checks can verify that two signatures are on the checks or the person doing the bank reconciliation can review the canceled checks or go on-line to verify that the dual signatures were done as required.

YOUR CHECK-SIGNING POLICY: EFFICIENCY VERSUS RISK

By Bart Beauchamp

When your association formulates or reviews its accounting policies, one matter that should be routinely visited is the check-signing requirement. Should your group have a dual signature policy? Some factors that may sway your decision are the size and type of your association, its operating budget, the number of service or product lines it offers and the experience level of your staff.

A Bank's Obligations. Many organizations require that two designated people sign checks, often times only for checks over a certain dollar amount. However, your association must ensure that this process is being followed because banks do not scrutinize signatures on checks and won't be held responsible for checks that clear without two signatures. For all accounts opened at a bank, a signature card is required. Banks rely upon signature cards for information on the nature of the organization or entity and the proper authority of those with signing capability. Your association, upon completing the signature card, is guaranteeing the truth of representation about your group and the way it intends to maintain that particular bank account, the genuineness of each signer on the account and that your association has read the depositor's agreement.

Most depositor agreements from banking institutions will state that when the bank takes an item for processing by automated means, it will not examine each item. A signature card will be obtained to verify signatures on a check only in cases when the check is presented at a branch location by a non-customer. If a check has two signature lines, the teller will also ascertain whether two signatures are required. If this is a service that is vital to your association, the bank's treasury or cash management department can provide services (such as positive pay) wherein checks clearing the bank will be scrutinized more thoroughly—but be prepared to pay additionally for these services.

Making the Choice: Efficiency Weighed Against Risk. When considering a one-signature or dual-signature policy, as in most business situations, it comes down to efficiency versus risk. The persons charged with the fiduciary responsibility of your group's fiscal well-being should contemplate this policy as deeply as any other accounting policy, weighing the benefits and faults of both check options.

The benefit of a one-signature requirement is efficiency; that is, decisions of payment are more prompt than in a dual-signature scenario. Bills may be paid expeditiously, which may be one possible way of gaining vendor discounts. The accounting staff member responsible for obtaining signatures need only track down or schedule one busy executive; with only one signer, that staff member can more quickly accomplish the task and move on to other duties.

There are a few risks of a one-signature policy: The chance of missing an error increases if only one set of eyes is reviewing the check; also, the chance of fraud increases dramatically. Dual-signature policies are usually instituted as a safety measure. But requiring dual signatures on every check may not be necessary. Imagine having to find two signers for a check that's needed immediately for something vital to your association's operation—and not having the availability of one of the signers. Also, if the second signer is not located on site, an employee may have to deliver the checks to the signer's location, which creates issues of security, extra costs and wasted time.

So which policy is correct? I recommend a blended policy. Require one signature for day-to-day expenses that are consistent in amount and timing. This will allow your association to run effectively. Then, require dual signatures for significant expenses. The amount that is considered significant will vary by organization and is usually based on materiality to the operating budget; for instance, for groups that operate on a $5 million budget, two signatures may be required on every check written for more than $10,000, possibly preventing losses due to error or fraud. This combination method can offer your association a satisfactory blend of both worlds: the efficiency of the single signature and the loss prevention of the dual signature. ■

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Dual-Signature Checking Accounts

Small businesses, non-profit charities, partnerships, co-executors and co-trustees sometimes use dual-signature checking accounts as an internal accounting control procedure. If not implemented carefully, these accounts can make banks liable when the customer's personnel fail to comply with the customer's internal dual authorization requirement. For this reason, some banks simply refuse to open dual-signature accounts, which frustrates customers and bankers alike. There are several ways banks accommodate these customers' needs without undue risk.

Modern-Day Check Processing and the UCC

To understand the issues involved requires a basic understanding of modern-day check processing and applicable sections of the Uniform Commercial Code (UCC). Until about forty years ago, banks manually verified all check signatures against account signature cards where requirements for multiple signatures were noted. As the number of checks increased and customers demanded faster transactions, check processing became automated. Today, automated systems process hundreds of checks per minute. It is not feasible to verify signatures on all these checks. Nor is signature verification an effective fraud prevention method because people's signatures change over time and high resolution scanning technology makes forging signatures easy and undetectable. Today, most banks use risk management programs and fraud filters to identify fraudulent checks, and only suspect checks are manually inspected.

Acknowledging industrywide acceptance of automated check processing, the UCC was revised to provide that "ordinary care" and "reasonable commercial practices" for banks processing checks by automated means do not require manual examination of checks if the bank follows prescribed procedures and does not vary unreasonably from general banking practices.[1] Accordingly, a bank that pays a dual-signature check with only one signature because the bank's automated check processing system did not verify there were two signatures likely will not be liable to the customer for negligence for failure to exercise ordinary care or reasonable commercial practices.

However, the UCC also provides that a bank may only charge the account of a customer for checks that are "properly payable," and that a check is properly payable if it is "authorized by the customer" and is in accordance with an agreement between the customer and bank.[2] The UCC further provides that, "[i]f the signature of more than one person is required to constitute the authorized signature of an organization, the signature of the organization is unauthorized if one of the required signatures is lacking."[3] While not necessarily negligent, a bank that pays a dual-signature check with only one signature is strictly liable for re-crediting the customer's account because the check is treated as having an "unauthorized signature" and is not "properly payable" and cannot be charged against the customer's account.

Product Options

There are several ways banks mitigate the risks associated with multiple signature checks. One way is by not offering dual-signature accounts, which may cost the bank some business. Another solution is offering a dual-signature checking account as a special product with procedures to manually inspect all checks written on the account. Additional fees are often charged to compensate for the manual processing and increased liability risk.

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[1] UCC § 3-103.
[2] UCC § 4-401.
[3] UCC § 3-403.

Other banks offer dual-signature accounts where the account contract clearly indicates that payment is authorized by a single signature, but that the face of the customer's checks will have two signature lines to accommodate the customer's internal dual-authorization procedures. According to one UCC expert, "[t]his type of provision should be enforceable under the freedom-of-contract principle codified in UCC § 4-103(a)," [4] which provides that the effect of the UCC provisions discussed above "may be varied by agreement" as long as the agreement does not limit a bank's responsibilities to act in good faith and exercise ordinary care. This type of agreement varies the effect of the UCC provisions discussed above such that a two-signature check signed by one person will be "authorized by the customer" and "properly payable" by the bank. The following statements should be included in the agreement:

- the bank processes claims on an automated basis, based on information encoded on checks;
- automated processing reduces costs, to the benefit of all bank customers;
- because of automated processing, the bank cannot compare signatures or determine that a dual-signature requirement is being violated;
- any dual-signature requirement is a matter that is internal to the customer, whether the bank knows of it or not;
- the customer cannot assert a claim against the bank for permitting a transaction that violates the customer's dual-signature requirement; and
- if the customer wants the bank to sight-review presented checks for violation of the customer's dual-signature requirement, it must give specific notice to the bank and pay a fee for the service.[5]

A checking account with "positive pay" features is yet another option offered by many banks. Positive pay is a fraud prevention tool where one customer representative has authority to sign checks, and another customer representative has authority to approve checks presented to the bank for payment. Checks not approved by the second individual upon presentment to the bank are not paid by the bank. Additional fees are often charged for these accounts to compensate for the additional systems and procedures and added liability risk.

Takeaways

One takeaway is that there are a variety of products offered by different banks, and customers should shop around to find the products or services that most closely align with their needs and preferences. Another takeaway is that banking laws and regulations should not treat banks as utilities that are required to offer commodity products and services. For banking products and services to evolve with technological advances and modern business practices, banking laws and regulations must encourage flexibility, creativity, and entrepreneurial innovation.

For more information about the dual-signature account matters discussed in this article, contact Mel Tull, VBA General Counsel, at mtull@vabankers.org or (804) 819-4710.

This article has been prepared for informational purposes only and is not legal advice.

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[4] See 2 Clark and Clark, *The Law of Bank Deposits, Collections and Credit Cards* (3d ed. 2014), § 10.02[2], p.10-30, for more information about this type of contractual provision.

[5] *Id.* at p. 10-31.