



CLIENT LOGIN

TREASURY RESOURCES

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ACH: Basics

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Objectives

- Provide a fundamental understanding of the ACH Network
- Understand the ACH applications and their applicability to business processes
- Clarify the Roles and Responsibilities of participants
- Be conversant in industry terms and concepts
- Review risk in ACH payments, and the ACH system



The ACH Network

- Electronic Payments Network
 - Batch processing, store-and-forward system
- ACH movement began in the late 1960s
 - Special Committee on Paperless Entries (Scope)
 - By 1972, regional ACH Associations were established
- The “real” push was the direct deposit of social security payments in the early '70's, followed by the direct deposit of payroll, from the private sector



The ACH Network

- The National Automated Clearing House Association (NACHA) was formed in 1974
 - NACHA changed its in 1999 to:
 - **NACHA – *The Electronic Payments Association***
- The inter-regional exchange was established in 1978, up to then, ACH could be like a batch listing of check payments (but without the checks), e.g. like the cash letter
- The ACH Network became “all electronic” in 1993
- 5 new ACH applications since Sept. 2000



ACH Terms

Key Participants

- Originator
- Originating Depository Financial Institution (ODFI)
- ACH Operator
- Receiving Depository Financial Institution (RDFI)
- Receiver
- Third-Party Processor



ACH Terms

- Addenda Record
- Authorization
- Banking Day
- Effective Entry Date
- Funds Availability
- Notification of Change
- Posting



ACH Terms

- Prenotification
- Returns
- Reversals
- Settlement
- Settlement Date
- Standard Entry Class Codes
- Transaction Codes



Standard Entry Class Codes

THE reason a payment is made comes first in ACH.....

ACK	CBR	DNE	PBR	RET	TRC
ADV	CCD	ENR	POP	RCK	TRX
ARC	CIE	MTE	POS	SHR	WEB
ATX	COR	NOC	PPD	TEL	XCK
	CTX				

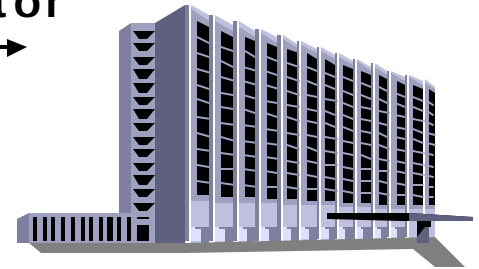
As opposed to a check, which is first a payment, then for a reason.



ACH Transaction Flow



Receiver authorizes the Originator

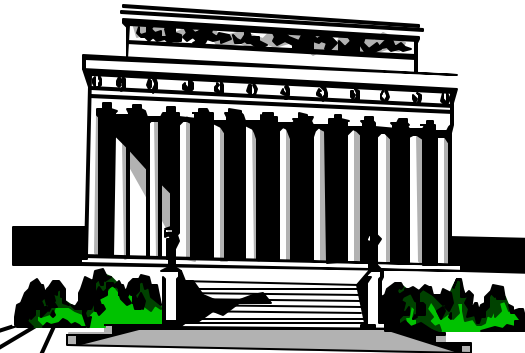


Receiver

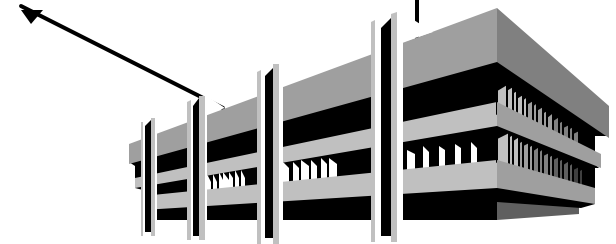
Originator



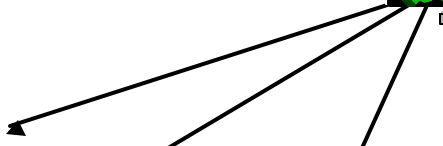
RDFI



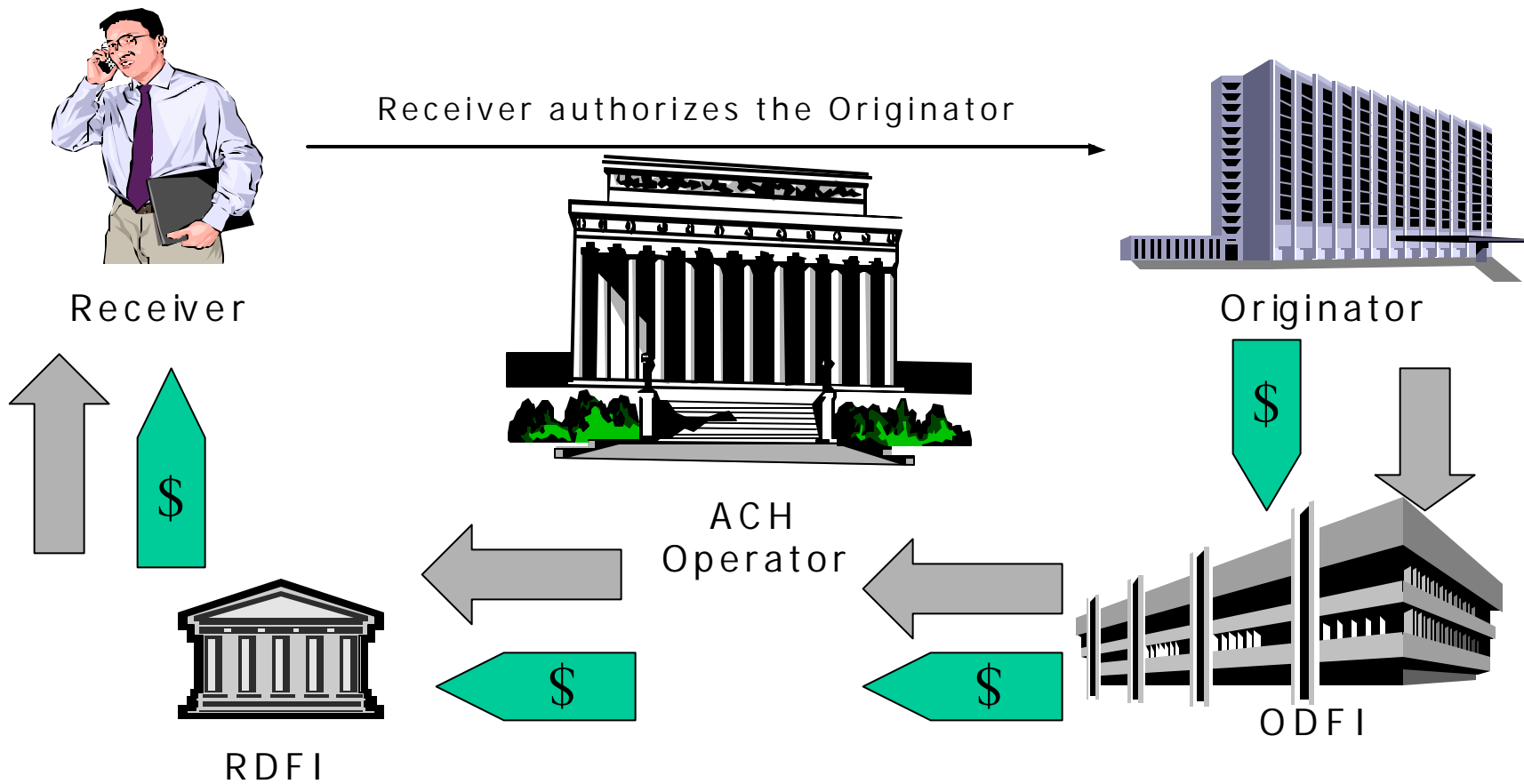
ACH
Operator



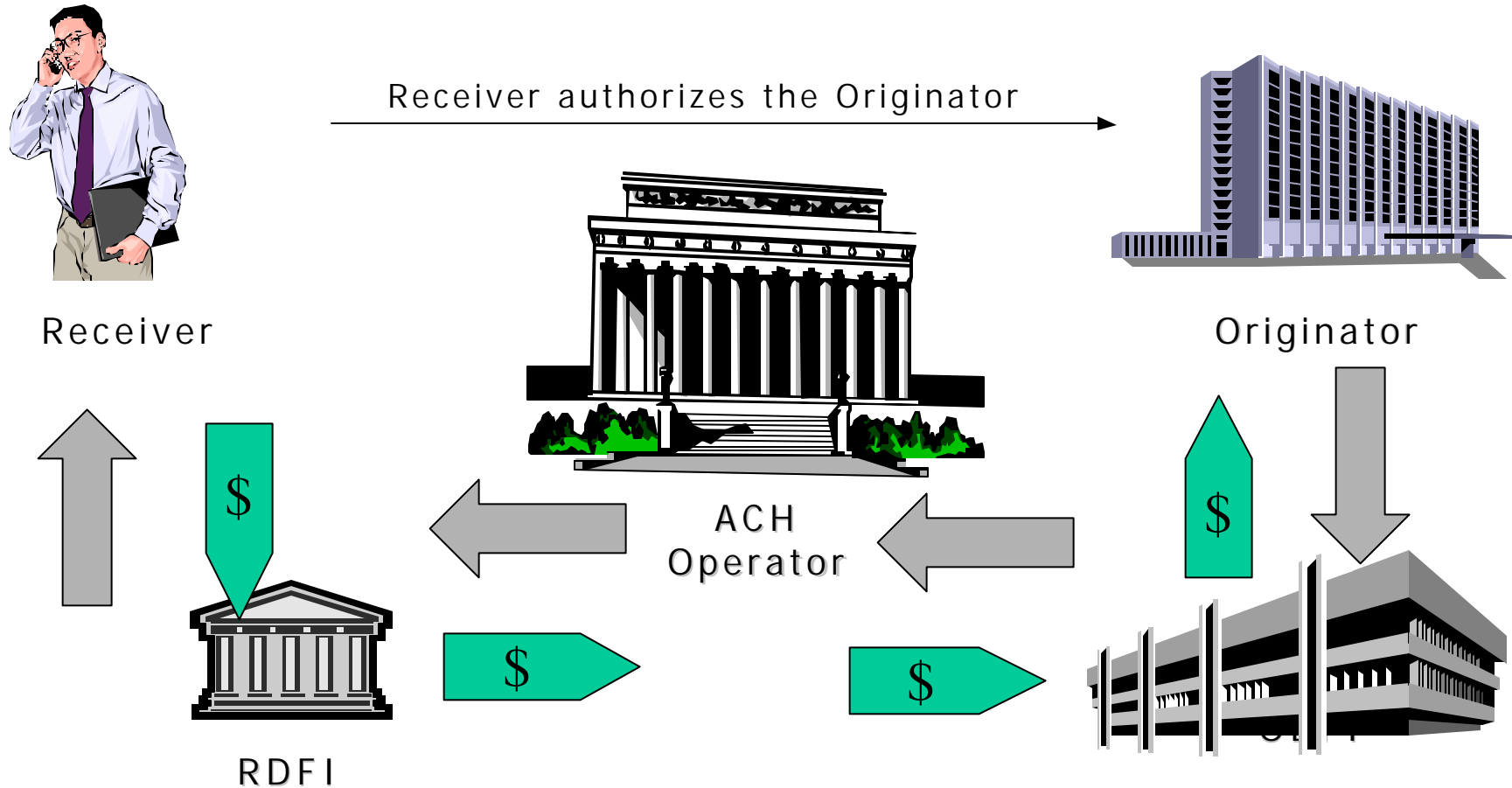
ODFI



ACH Credit Flow



ACH Debit Flow



Rules and Regulations

- ACH Operating Rules
- Electronic Funds Transfer Act / Regulation E
- Uniform Commercial Code Article 4A
- OFAC
- Operating Circulars of the Federal Reserve System
- State Law



Rules and Regulations

- Uniform Commercial Code Article 4
- Federal Regulation CC
- Federal Regulation D
- The Right to Financial Privacy Act
- Gramm-Leach-Bliley
- US Patriot Act



Originator Responsibilities

- Execute Agreement With ODFI
 - Details Rights & Responsibilities of parties to agreement
 - Binds Originator to the ACH Operating Rules
 - Acknowledges that entries may not violate the laws of the United States (OFAC)



Originator Responsibilities

- Obtain Authorizations
 - Consumer Credit – Orally or by other non-written means
 - Consumer Debit – in writing, signed or similarly authenticated
 - Unique Authorization Scenarios: XCK, RCK, TEL and ARC
 - Except for POP, TEL, ARC and WEB single entry – Originator must provide Receiver with information to revoke authorization
 - Corporate Credits/Debits (CBR, CCD, CTX) – Receiver has agreement with Originator
- Exception to Authorization Requirement



Originator Responsibilities

- Retain Authorizations for Two Years From Termination
- Provide Notice to Consumer Receiver if Amount or Scheduled Debit Date Changes
 - If amount changes notice required 10 calendar days prior to date entry is to be initiated
 - If date changes notice required not less than 7 calendar days prior to new scheduled debit date



Originator Responsibilities

- Send Prenotes, if desired
 - Prenotes are optional for all ACH transactions
 - Six banking day rule applies if Prenotes are initiated



ODFI Warranties

- Agreements are Executed
 - ACH Operator
 - Originator
 - Third-Party Processor
- Exposure Limits Established
 - Review limits periodically
 - Monitor across multiple settlement dates
 - Special risk considerations for CBR, PBR, WEB and TEL entries



ODFI Warranties

- Entries are Authorized
- Terminating Entries When Appropriate
 - Authorization Revoked
 - Termination by Operation of Law
- Timeliness of Entries
- Transmittal of Required Information
- Audit and Compliance for Origination of ACH Entries
 - Ensure that Originators are kept informed



RDFI Obligations

- Verify Prenotifications
- Accept Entries
- Reliance on Account Number for Posting
- Receipt of Entries
 - Availability of Credit Entries
 - Posting of Debit Entries
- Provide Payment Remittance Information



RDFI Obligations

- Reliance on SEC Codes
- Disclosure Requirements
 - Periodic Statement
 - UCC 4A Disclosure
- Right to Return Entries
 - “Written Statement Under Penalty of Perjury” Requirements
- Audit Compliance with ACH Rules



Rights of Receivers - Consumer

- Credit entries available on Settlement Date
- Debit entries posted no earlier than Settlement Date
- Right to reaccredit for unauthorized debits
 - 60 days from statement date (Reg E)
 - Waiver of right to recredit
- Periodic Statement information
- Stop Payment



Rights of Receivers - Corporate

- UCC 4-A
 - Disclosure
- Stop Payment
- Unauthorized debit
 - Deadlines
 - Recredit
- Remittance Information
- Acknowledgements



Returns of Entries

- Returns must be made available to the ODFI by opening of business on the second banking day following the Settlement Date of the Original Entry
- Only the exact dollar amount of the original entry may be returned
- Must use valid return reason
- Return the same TYPE of entry (credit/debit)
- Return all information sent in the original entry
- Return entry records must be retained for SIX years



Dishonored Return

- Originator may have ODFI dishonor a return if:
 - The entry has been returned later than the deadline established for accepting returns
 - AND, either the Originator or the ODFI has suffered a loss
 - The return entry contains incorrect information
- Dishonored Return must be sent to the RDFI within 5 banking days of the settlement date of the Return



Contested Dishonored Return

- RDFI initiates a Contested Dishonored Return entry:
 - If based on an untimely return entry, which was in fact timely
 - ODFI Dishonored Return was untimely
- Must be transmitted to ACH Operator within 2 Banking days after Settlement Date of Dishonored Return
- ODFI Must Accept; May not contest a Contested Dishonored Return

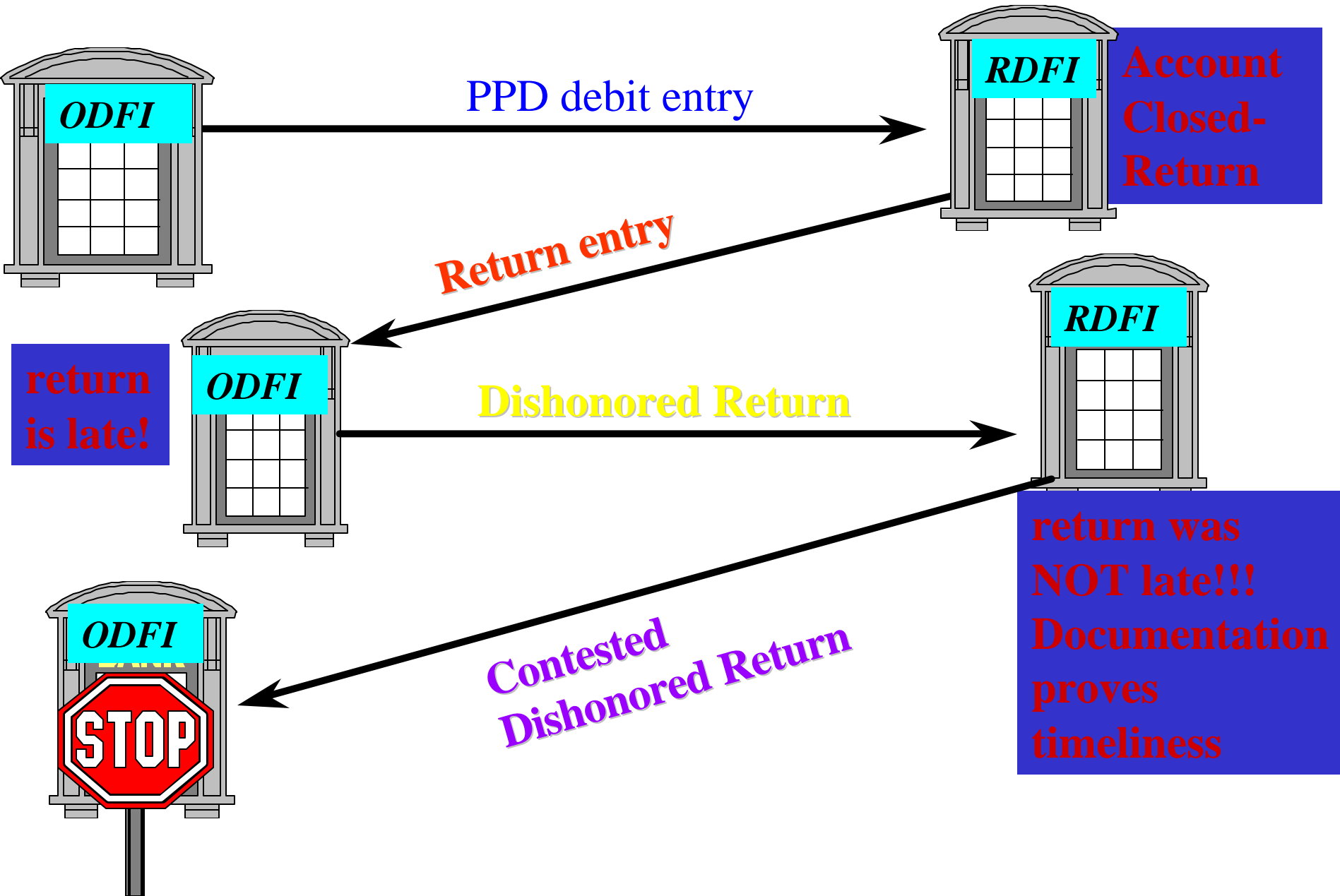


Corrected Dishonored Return

- RDFI initiates a Corrected Dishonored Return entry:
 - ODFI Dishonors a Return containing incorrect information
- Must be transmitted to ACH Operator within 2 Banking days after Settlement Date of Dishonored Return



ACH Return Item Flow



Notifications of Change (NOC)

- Non-dollar entry sent by an RDFI to correct information received in a Prenote or live entry
- RDFI warrants that information is correct
- Unique SEC code - COR
- Distributed back to the Originator through the ODFI



Notifications of Change (NOC)

■ RDFI Action

- Initiated and transmitted within 2 banking days of receipt of entry to which it relates
- Warranties and Indemnification
 - Information contained in NOC is correct
 - Change related to Receiver's account number
 - Receiver has authorized the change
 - RDFI warranty supersedes the ODFI warranty
 - Indemnifies each ODFI, ACH Operator and Association



Notifications of Change (NOC)

■ ODFI Action

■ Provide NOC information to Originator

- Within 2 banking days of settlement date of NOC
- Minimum information
 - Company Name, Company Identification, Company Entry Description, Effective Entry Date, Account Number, Individual Name, Individual Identification Number, NOC Change Code, Original Entry Trace Number, RDFI Routing Number, Corrected Data



Notifications of Change (NOC)

- Originator Action
 - Make the specified changes within 6 banking days of receipt of the NOC information
 - OR, prior to initiating another entry, whichever is later



ACH Operator Rejects

- ACH Operator edits all entries and returns those that cannot be processed
- Unique Return Codes used by ACH Operators
- Indicates that the rejected entry was not successfully processed through the ACH system



Reversing Files

- Originated to reverse an entire file of entries that were either duplicated or erroneous
- Must be initiated within five banking days of settlement date of duplicate or erroneous file
- 'REVERSAL' contained in Company Entry Description field of Company Batch Header
- Corrected file should be initiated with reversing file



Reversing Entries

- Debit or credit to correct a previous erroneous credit or debit
 - 5 banking days
- An erroneous entry is:
 - duplicate of an entry previously initiated; or
 - orders payment to or from a Receiver not intended to be debited or credited by the Originator; or
 - orders payment in a dollar amount different than was intended by Originator



Reversing Entries

- The Originator of a reversing entry must notify the Receiver that:
 - a reversing entry has been transmitted to the Receiver's account
 - include the reason for the reversing entry
 - no later than Settlement Date of the reversing entry
- Method of notice determined by Originator



Types of Risk

- Credit
- Fraud
- Operational
- Systemic



Credit Risk

■ Credit entries:

■ Exposure for ODFI based on -

- Time (temporal risk)
 - two day credit window
 - overnight risk
- Funding method (internal, check, wire, ACH, etc.)
- Credit quality of customer
- Value of batch/file
- Use of third party processor

■ Exposure of RDFI based on -

- Third party processor



ACH Credit Risk (continued)

■ Debit Entries:

■ Exposure for ODFI based on -

- Time (temporal risk)
- Exception entries (returns)
- Credit quality
- Value of batch/file
- Value of collateral (if any)

■ Exposure of RDFI based on -

- Third party use
- Returning debits timely



Product Based Credit Risk Issues

- Credit products:
 - Direct deposit
 - Corp. cash disbursement
 - Business to business payments
- Debit products:
 - Direct payment
 - Cash concentration
 - Business to business payments



ACH Fraud Risk

■ What is it?

■ *External*

- disk, list, etc.
- data transmission
- altered or fraudulent

■ *Internal*

- fraudulent file, batch, or entry
- Alteration of company file, batch, or entry



Operating Risk

- What is it?
 - Hardware failure
 - Software failure
 - Telecommunications failure
 - Power failure
 - Human error
 - Staffing problems, issues
 - Disaster
 - Third parties



Managing Operating Risk

- Secure storage
- Limited access for personnel
- Dual control
- Back-up copies
- Audit trails
- File balancing
- File accountability or confirmations
- System maintenance/evaluation
- Well tested software enhancements
- Alternate telecommunications systems
- Alternate power source
- Employee training
- Contingency planning



Disaster Recovery

- What is key?
 - A plan (that considers as many possibilities as possible)
 - Test the plan!!!!
- Approaches most often taken
 - Back-up sites/hot sites
 - Telecommunication back-ups
 - Regular testing of the plan (real life works best) and regular reviews of that plan
 - Cross-trained staff, well documented procedures
- Another issue for ACH – Excused delay



Systemic Risk

- “Domino” effect
- Monitored by the Federal Reserve System
 - Daylight overdraft limits
 - De Minimis Cap
- TIED TO FINALITY
 - When funds CANNOT be taken back
 - Today - Opening of Bus. the day AFTER settlement day
 - 2001 - Opening of Bus. on settlement day



Third Party Risk

- YOUR R/T# IS ON THE FILE - YOU ARE RESPONSIBLE!
 - Be sure you have a contract with any third parties
 - Your contractual obligations should include:
 - All companies have a signed contract with you and the vendor
 - File limits are set and monitored, over-limit procedures in place
 - Monthly statistics are delivered to you by vendor
 - Audit requirements for 3rd parties beginning in 2000
 - Liabilities and warranties if something is done incorrectly
 - Termination rights
 - Delivery of files



Settlement, Availability, and Finality

■ Settlement

- Only through Fed Accounts
- Fed determines settlement day (Julian format)
- Settlement date vs. effective entry date

■ Availability

- Credits - opening of business
- Debits - 10:00 A.M. local time
- MAY effect your intra day cap
- What is your availability to your customers?

■ Finality

- Credits - opening of business the day after settlement day
- Debits - ??



For more intense information...or to shape the ACH System:

- NACHA Membership:
 - Members: Banks & ACH Operators
 - Affiliate Members: "any organization interested in the quality of the ACH network"
- The AAP (Accredited ACH Professional) similar to the CCM, as a certification as to mastery of a body of knowledge, with education credits thereafter for continued certification
- NACHA's Councils:
 - Electronic Check Council
 - Council for Electronic Billing & Payment
 - Electronic Benefits Services Council
 - Global Payments Forum
 - Internet Council

