

# ACH BASICS

# AN ACH PRIMER

This is designed to provide those who are not familiar with the ACH Network with a basic understanding of the fundamentals of the ACH Network.

# ACH NETWORK OPERATION

- ❑ The ACH Network is a batch processing, store and forward system.
- ❑ Transactions received by the financial institution during the day are stored and processed later in a batch mode.
- ❑ ACH transactions are accumulated and sorted by destination for transmission during a pre-determined time period.
- ❑ This provides faster processing than paper checks.
- ❑ ACH transactions are transmitted electronically between financial institutions through data transmissions.

# HISTORY OF THE ACH NETWORK



# History of the ACH Network

- ▣ Began in the early 1970's when a group of California Bankers formed the Special Committee on Paperless Entries (SCOPE).
- ▣ This committee explored the technical, operational and legal framework necessary for an automated payments system.
- ▣ The ACH association began operation in 1972 and led to the formation of similar groups in other parts of the country.
- ▣ The National Automated Clearing House Association (NACHA) was formed in 1974 to coordinate the ACH movement nationwide.
- ▣ In 1978, local ACH's were linked electronically on a nationwide basis.



# NACHA

- ▣ NACHA's primary roles:
  - Develop and maintain the NACHA Operating Rules
  - Promote growth in ACH volume
  - Provide educational services to its members and other ACH participants
  - NACHA also:
    - ▣ Serves over 15,000 financial institutions across the U.S.
    - ▣ Over 7 billion businesses use the ACH Network
    - ▣ Estimated \$145 Million consumers use the ACH Network
    - ▣ Approximately \$15 Billion payments are processed annually

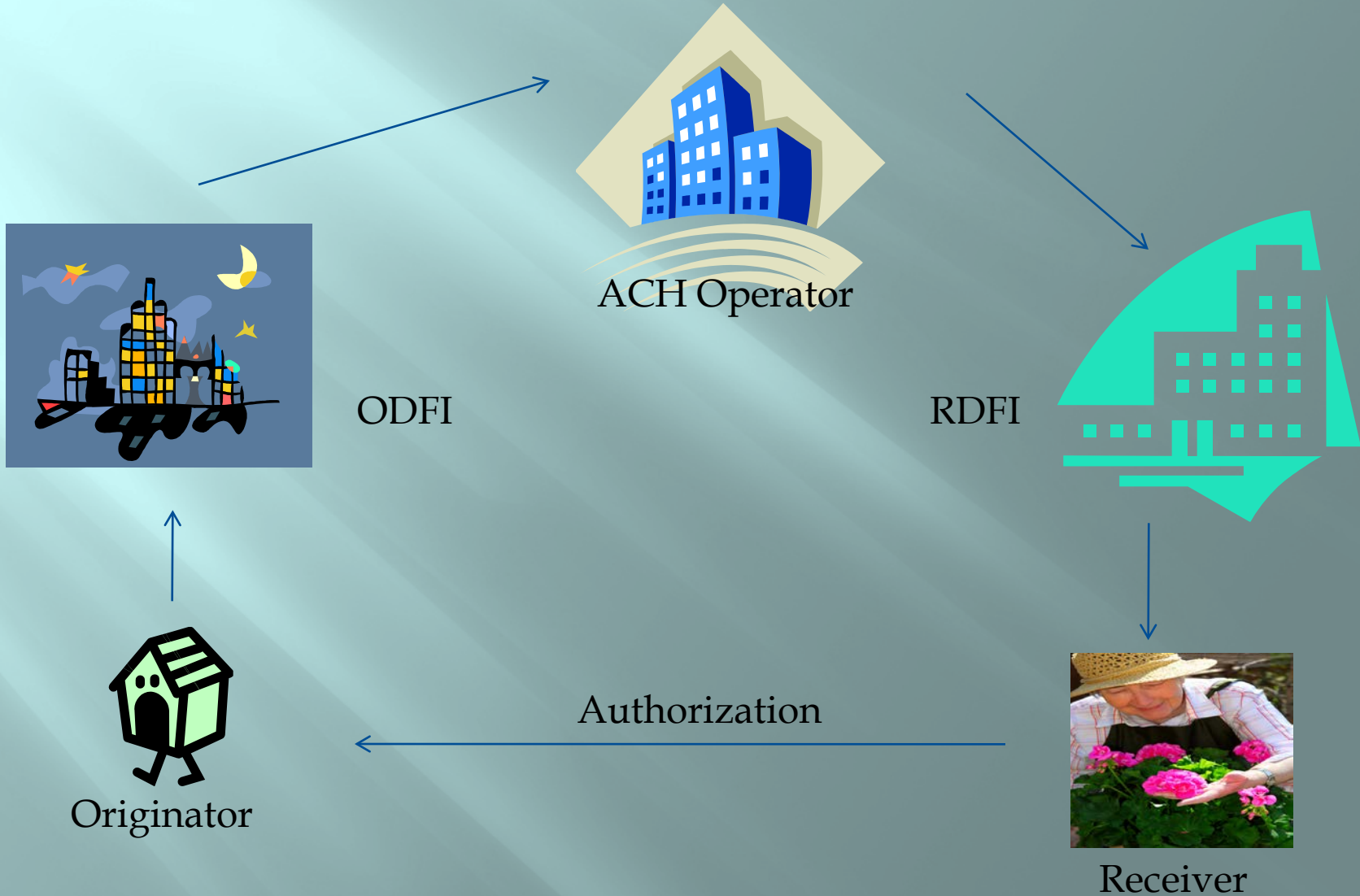
# Regional Payment Associations

- ▣ Regional associations provide management, education, assistance to commercial banks across the U.S.
- ▣ Develop and implement local ACH rules that apply specifically to their member financial institutions
- ▣ Offer a wide variety of educational sessions

# PARTICIPANTS



# PARTICIPANTS



# PARTICIPANTS



ORIGINATOR

- ▣ Agrees to initiate ACH entries according to an arrangement with a Receiver.
- ▣ Usually a company directing a transfer of funds to or from a consumer's or another company's account.
- ▣ The originator could be an individual also but could also be Federal or State Government.

# PARTICIPANTS

- ▣ This is the institution that receives payment instructions from an Originator to forward entries to the ACH Operator.



**ODFI**  
**ORIGINATING DEPOSITORY**  
**FINANCIAL INSTITUTION**

# PARTICIPANTS



**ACH OPERATOR**

- ▣ The central clearing facility operated by a private organization or the Federal Reserve Bank on behalf of Depository Financial Institutions to transmit or receive ACH entries.
- ▣ There could be two operators involved in any transaction, one as the originating operator and another as the receiving operator.

# PARTICIPANTS

- ▣ The Depository Financial Institution that receives ACH entries from the ACH Operator and posts the entries to the accounts of it's depositors (Receivers).



**RDFI**  
**RECEIVING DEPOSITORY**  
**FINANCIAL INSTITUTION**



# PARTICIPANTS

- ▣ A natural person or an organization which has authorized an Originator to initiate an ACH entry to the Receiver's account with the RDFI.
- ▣ A Receiver may be either a company or a consumer depending on the type of transaction.



**RECEIVER**

# PARTICIPANTS

- ▣ In some instances, an originator, ODFI or RDFI may choose to use a Third-Party Service Provider for all or part of the process of handling ACH items.
- ▣ This is an entity that performs the functions on behalf of the originator, ODFI or RDFI.
- ▣ This can include the creation of ACH files or just acting as a sending or receiving point on behalf of an ODFI or RDFI.

# ACH TRANSACTION FLOW

- ▣ Unlike a check, an ACH entry may be either a credit or a debit entry.
- ▣ If the Receiver's account is debited, than the entry is an ACH Debit.
- ▣ If the Receiver's account is credited, than the entry is an ACH Credit.
- ▣ Conversely, the offset to an ACH debit is a credit to the Originator's account and the offset to an ACH credit is a debit to the Originator's account.

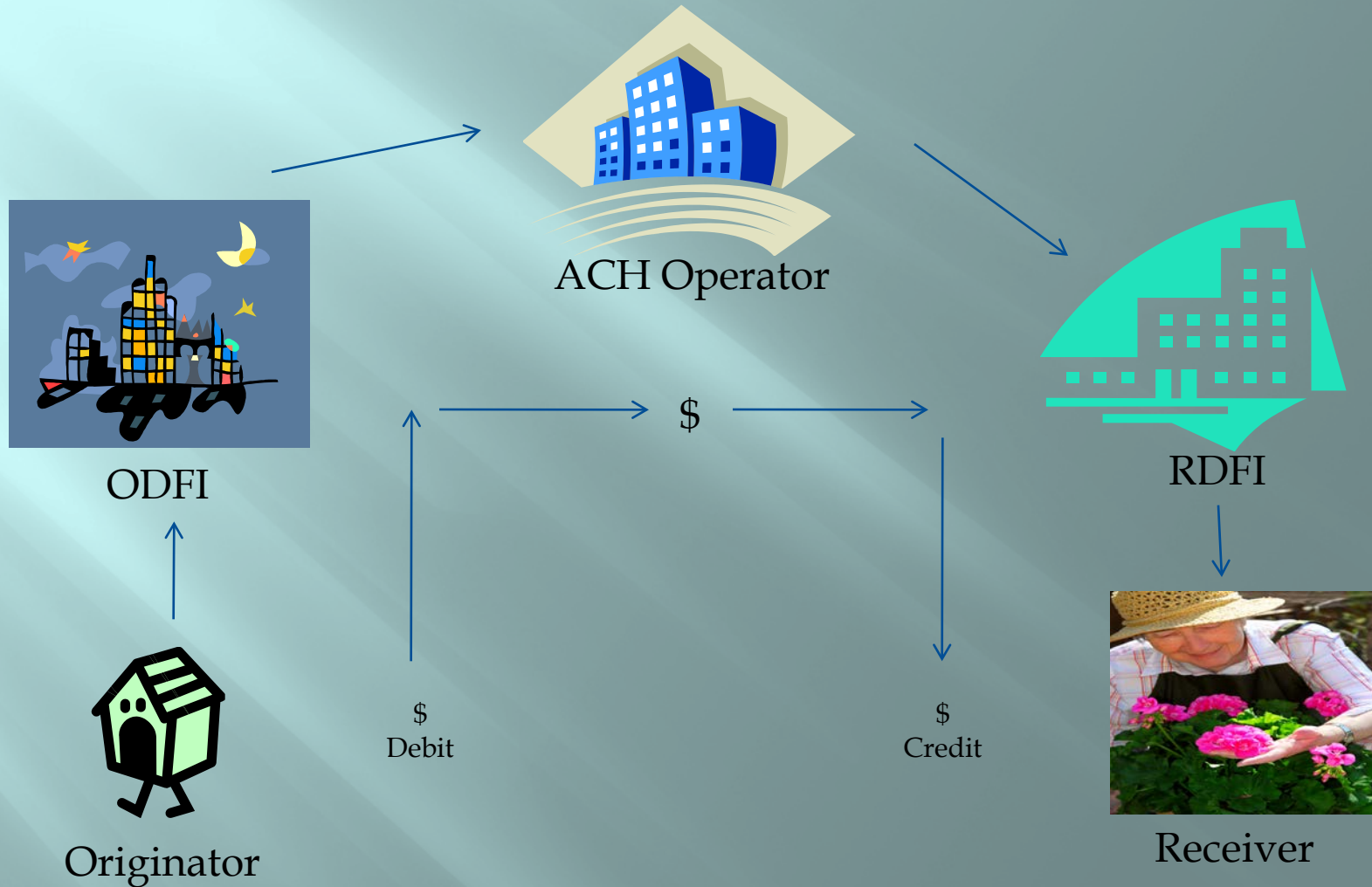


# ACH CREDITS

- ▣ ACH credits involve both consumer and corporate payments with separate rules and regulations for each. The most common ACH credit is payroll
- ▣ Common ACH Credits
  - Annuities
  - Customer-initiated transactions (telephone bill payments)
  - Corporate-to-corporate payments
  - Dividends
  - Interest Payments
  - Payrolls – private and government
  - Pensions – private and government
  - Social Security payments
  - Tax Payments
  - Government Vendor Payments



# ACH Credit Flows



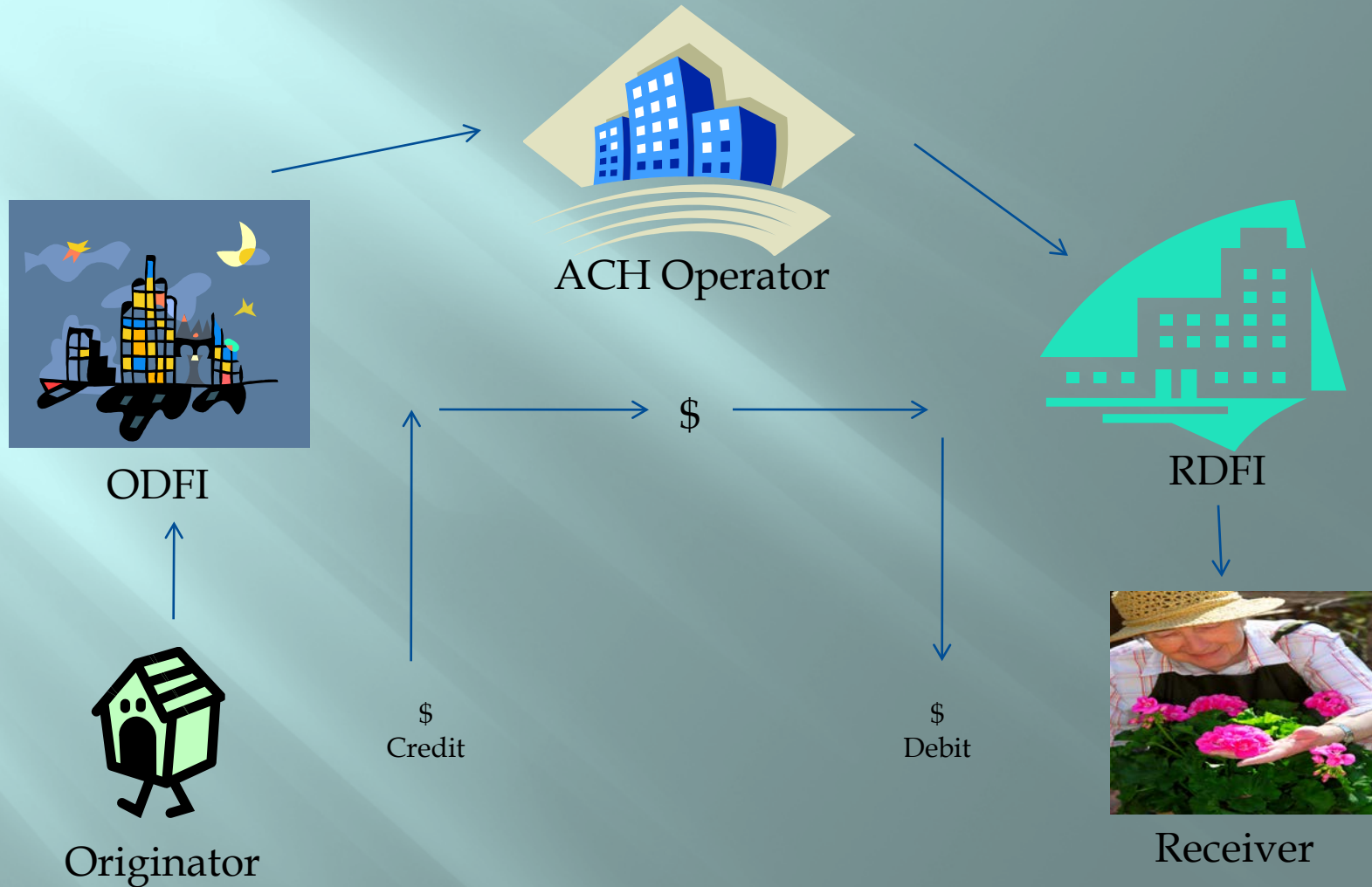
# ACH Credit Flows

- ▣ A payroll deposit credit flows from an account at a company's financial institution to an account at an employee's financial institution.
- ▣ Credit entries must be posted to a Receiver's account no later than Settlement Date.
- ▣ Consumer entries that are made available to the RDFI by its ACH Operator by 5:00 p.m. (RDFI's local time) on the banking day prior to Settlement Date must be made available to the Receiver by opening of business on the Settlement Date.

# ACH DEBITS

- ▣ Funds are collected from a Receiver's account and transferred to an Originator's account (even though the Originator initiated the entry). Most common would be cable or electricity payments.
- ▣ Common ACH Debits
  - Association/Club dues
  - Cash Concentration
  - Distributor/dealer payments
  - Contributions to IRA's, 401(k)'s, etc.
  - Government Savings Bond purchases
  - Insurance payments
  - Mortgage and Installment loan payments
  - Utility payments
  - Tax Payments
  - Charitable donations

# ACH Debit Flows



# ACH Debit Flows

- ▣ For example, a preauthorized mortgage payment flows from a consumer's account at a financial institution to a mortgage company's account.
- ▣ Debit entries must not be posted to a Receiver's account prior to the Settlement Date.



# TYPICAL TRANSACTION FLOW

- ▣ The Originating Depository Financial Institution (ODFI) and the originating company determine, by agreement, how the information must be delivered to the ODFI.
- ▣ The ODFI establishes processing schedules and cutoff times with its Originators so that entries may be processed and transmitted in sufficient time for settlement to occur on the dates desired by its Originators.
- ▣ The Company delivers the file to its ODFI
- ▣ The ODFI generally removes “on-us” entries and transmits the remaining entries to the originating ACH Operator by the deadline.
  - “On-us” transactions are ones in which the Receiver and the Originator both have accounts at the same Financial Institution so is not initiated into the ACH Network.
- ▣ The ACH Operator sorts the entries by RDFI routing number and transmits the payment information to the appropriate RDFI’s for posting.
- ▣ On Settlement Date, all parties to the transaction effect the appropriate settlement of funds.

# CONSUMER PAYMENTS



- ❑ Consumer payments include credit's such as payroll, retirement, dividends, interest and annuity payments.
- ❑ They include debit's such as insurance premiums, mortgage payments, utility payments, installment payments membership dues.
- ❑ The ACH network is also used to settlement consumer transactions made at ATM's and Point-of-sale terminals

# CORPORATE PAYMENTS

- ❑ Corporate payments include cash concentration and disbursement, corporate trade payments and Federal Tax payments and financial electronic data interchange (EDI).
- ❑ Cash concentration and disbursements allows companies to achieve efficiencies in cash management.
- ❑ Corporate trade payments enables corporations to exchange both data and funds with trading partners.





# PAYMENT APPLICATIONS

- ▣ In specific cases, a particular application may be used for both consumer and corporate transactions.
- ▣ Each ACH application is identified and recognized by a specific Standard Entry Class Code (SEC Code) which appears in the ACH record format.
- ▣ The SEC Code also identifies the specific computer record format that will be used to carry the payment and payment related information relevant to the application.
- ▣ Ach entries may be transmitted to a variety of account types
  - Demand accounts
  - Savings accounts
  - Financial institution general ledger accounts
  - Loan accounts (credit entries only)

# CONSUMER SEC CODES

- ▣ CIE – Customer Initiated Entry
  - Limited to credits where a consumer initiates the transfer of funds to a company through some type of home banking product or bill payment service provider.
- ▣ MTE – Machine Transfer Entry
  - The ACH Network supports the clearing of transactions from ATM's
- ▣ PPD – Prearranged Payment and Deposit Entry
  - Direct Deposit – a credit application that transfers funds into a consumer's account at the RDFI and represents a variety of products such as payroll, pension, etc.
  - Preauthorized Bill Payment – a debit application; the consumer grants the company authority to initiate periodic charges to the consumer's account as bills become due such as insurance premiums, utility payments.



# CONSUMER SEC CODES

- ▣ POS/SHR – Point of Sale Entry/Shared Network Transaction
  - These two represent point of sale debit applications in either a shared (SHR) or non-standard (POS) environment. These are most often initiated by the consumer via a plastic access card (Debit Cards).
- ▣ RCK – Re-presented Check Entry
  - A single-entry ACH debit application used by Originators to re-present a check that has been returned to them as insufficient or uncollected funds. This provides Originators with the potential for improvements to processing efficiency and decreased collection costs.

# CONSUMER SEC CODES

- ▣ TEL – Telephone Initiated Entry
  - Used for the origination of a single-entry debit transaction to a consumer's account by oral authorization obtained from the consumer via the telephone. This type of transaction may only be originated when there is either:
    - ▣ An existing relationship between the Originator and the Receiver, or
    - ▣ No existing relationship between the Originator and the Receiver, but the Receiver has initiated the telephone call.
- ▣ WEB – Internet Initiated Entry
  - Used for the origination of debit entries (can be recurring or Single-Entry) to a consumer's account pursuant to an authorization that is obtained from the Receiver through the internet.

# CORPORATE SEC CODES

- ▣ CCD – Corporate Credit or Debit
  - This can be either a credit or debit where funds are transferred between unrelated corporate entities or transmitted as intra-company cash concentration and disbursement transactions.
- ▣ CTX – Corporate Trade Exchange
  - Supports the transfer of funds (debit or credit) within a trading partner relationship in which a full ANSI ASC X12 message or payment related UN/EDIFACT information is sent with the funds transfer. This data is placed in multiple addenda records.

# CONSUMER AND NON-CONSUMER SEC CODES

- ▣ ARC – Accounts Receivable Entry
  - Enables Originators to convert to a Single-Entry ACH debit an eligible check received through the mail or a dropbox location for a payment of goods or services.
- ▣ BOC – Back Office Conversion Entry
  - Enables Originators (during back office processing) to convert to a Single-Entry ACH debit an eligible check received at the point of purchase or manned bill payment location for the in-person purchase of goods or services.
- ▣ IAT – International ACH Transaction
  - Identifies an ACH credit or debit entry that is part of a payment transaction that involves a financial agency's office that is not located within the U. S. These transactions convey information to ensure that all parties to the transaction can comply with the U.S. law which includes the programs administered by the Office of Foreign Assets Control (OFAC).



# CONSUMER AND NON-CONSUMER SEC CODES

- ▣ POP – Point of Purchase Entry
  - Used by Originators as a method of payment for the in-person purchase of goods or services by Receivers. These Single-Entry debit entries are initiated by the Originator based on a written authorization between the Originator and the Receiver and notice provided by the Originator at the point of purchase or manned bill payment location. The source document (typically a check) is voided by the merchant and returned to the Receiver at the point-of-purchase.



# OTHER SEC CODES

- ▣ ACK/ATX – Acknowledgement Entries
  - Are available for use by the RDFI to acknowledge receipt of ACH credit payments originated using the CCD or CTX formats
- ▣ COR – Automated Notification of Change or Refused Notification of Change
  - Used by an RDFI or ODFI when originating a Notification of Change or Refused Notification of Change in automated format.
- ▣ DNE – Death Notification Entry
  - Utilized by a Federal Government agency to notify a depository financial institution that the recipient of a government benefit payment has died.
- ▣ ENR – Automated Enrollment Entry
  - Allows a depository financial institution to transmit ACH enrollment information to Federal Government Agencies via the ACH Network for future credit and debit applications on behalf of both consumers and companies.

# OTHER SEC CODES

- ▣ XCK – Destroyed Check Entry
  - Utilized by a collecting institution for the collection of certain checks when those checks have been destroyed.

# ADVANTAGES TO PARTICIPANTS





# Advantages to Consumers



- ▣ Direct Deposit benefits to recipient
  - Elimination of time and cost involved in depositing checks
  - Availability of funds on a timely basis, even on vacation or illness
  - Elimination of the possibility of lost or stolen checks
- ▣ Debit application benefits to the consumer
  - Do not have to write checks
  - Eliminate postage expense and risk of late payments
  - Avoid late or interest charges
  - Establishment of excellent payment and credit records

# Advantages to Companies

- ❑ Reduce administration and operating expenses
- ❑ Elimination of time lost by employees who deposit checks during working hours
- ❑ Reduction of clerical cost for account reconciliation
- ❑ Elimination of stop payment charges or check reissue costs
- ❑ Reduce paper handling costs
- ❑ Accelerated availability of funds
- ❑ Better cash management forecasting
- ❑ Improved business relationships
- ❑ Certainty of delivery
- ❑ Possible reduction of bank service charges





# Advantages for the ODFI



- ▣ Reduction of costs through increased automated processing
- ▣ New opportunities for increased business through expanded services
- ▣ Enhanced public recognition through provision of effective, efficient, and innovative payment services

# Advantages to the RDFI

- ▣ Reduction of costs through automated processing of electronic entries and elimination of handling individual items
- ▣ Alleviation of teller-line congestion during peak periods
- ▣ Ability to offer improved services to both consumer and corporate account holders
- ▣ Enhanced public recognition through provision of effective, efficient, and innovative payment services



# SETTLEMENT AND POSTING

- ▣ Settlement is the actual transfer of the value of funds between financial institutions to complete the payment instruction of an ACH entry.
- ▣ Provided by the Federal Reserve and private sector ACH Operators
- ▣ Federal Reserve calculates the net debit and credit positions of financial institutions and applies those credit and debits to the reserve accounts of the financial institution

# CONCLUSION

The ACH Network continues to grow with the development of payment opportunities for both consumers, corporations, and financial institutions.

Rules and regulations also continue to be developed and enhanced to ensure the integrity and safety of the funds being transferred between entities.