



## Is ACH Origination Right for Your Institution?

### Overview

The ACH Network is an efficient, cost effective, safe, and reliable payment network that allows funds to be electronically debited or credited to checking, savings, general ledger accounts, and credits to loan accounts. Acting as an Originating Depository Financial institution (ODFI) is part of most financial institution's core services. Currently, the U.S. Payment System is going through tremendous changes based on new technology and end-user expectations. Same Day ACH and Real-Time Payments are now a reality. To keep pace with the everchanging landscape, ACH origination should be a priority within your institution's strategic plan. The purpose of this document is to bring to your attention the many benefits, opportunities, and related risk in offering ACH origination services to corporate and small business customers. According to NACHA, ACH volume in 2017 exceeded 21.5 billion transactions valued at \$46.8 trillion. This volume translates to more than 66 transactions per person in the United States. If your institution is not offering ACH origination, your customers are looking elsewhere for this service. Be your customers' first choice when it comes to payment services.

### Safety and Security of the ACH Network

Since 1974, the ACH Network has provided a safe and secure method for financial institutions to move transactions. As with all banking services, ACH origination is not without risk, but with appropriate systems and controls, risk can be substantially mitigated and can provide deposit growth and income opportunities for your institution. The ACH Network is governed by the *NACHA Operating Rules and Guidelines*; each participant must follow the *Rules* which ensures consistency of processing. The ACH Network operates on a series of agreements with a foundation of common contract law and minimum language requirements. The *Rules* focus on many areas of risk management; these efforts ensure that the ACH Network remains one of the safest available means of moving payments and information. Ensuring the safety and security of all ACH network payments has been a collaborative effort between NACHA and the Regional Payments Associations. NACHA has implemented a Risk Management Strategy that encourages innovation and growth while focusing on and minimizing risk. Since implementing this strategy, the Network has experienced a significant decrease in unauthorized debits along with a dramatic increase in transaction volume. The strategy incorporates the importance of "Know Your Customer", proper due diligence, strong internal controls, *Rules* enforcement, monitoring return thresholds, implementation of a risk management program, completion of audits and risk assessments, and registration of Direct Access participants and Third-Party Sender relationships.

### Benefits and Opportunities of ACH Origination

**Convenience & Speed:** ACH is a faster payment method that can omit the use of paper checks or can speed the settlement process by converting paper checks to electronic transactions. ACH processing can provide businesses with greater/faster funds availability, pay employees quicker, reduce costs on postage, and transportation of checks for deposit and labor.

**Customer Expectation and Loyalty:** Corporate customers expect ACH origination services to be offered by their financial institution. Offering ACH origination allows financial institution's to grow and maintain their customer base. ACH origination offers a number of benefits to your corporate customers including, but not limited to, effectively managing their payables and receivables process, forecasting, and processing payroll. With the benefits comes customer loyalty.



**Deposit Growth:** ACH services can aid a financial institution in deposit growth. Institutions that offer ACH origination services are more appealing to prospective customers. Corporate/business customers need more efficient, cost effective, faster ways to pay employees and vendors. Corporate/business customers are more inclined to move their funds to an institution that meets all their financial and payment needs.

**Fee Income Opportunities:** Financial institutions have the tendency to feel they must give ACH services away for free. Visit Exhibit A of this document to review our profitability calculator to determine if offering ACH services will bring fee income to your institution. Consider charging originators a monthly fee, transaction fee, fees for servicing Third-Party Sender relationships, fees for Same Day ACH, and International ACH Transactions, etc. Corporate customers will pay for services that save them time and provide convenience.

**Lower Costs:** Processing ACH payments can cost less than alternatives such as debit/credit cards, wire transfers, and checks. ACH payments may also be one of the least expensive payment methods for originating payments compared to wire transfers and checks. ACH payments provide merchants with faster funds availability. According to a survey performed by Bottomline Technologies and the Association of Financial Professionals in 2017, the approximate median cost to issue a paper check is \$3.00 and to receive a paper check is \$1.57 whereas the approximate median cost to initiate and/or receive an ACH transaction is \$0.30.

**Payment Types:** The ACH Network offers many different payment types which are identified by the Standard Entry Class (SEC) code. The *NACHA Operating Rules* apply to each entry based on the SEC code being used. While financial institutions must receive most SEC Codes, the financial institution can select specific codes for ACH origination based on their risk appetite and customer demand.

**Recurring Payments:** With recurring ACH payments, customers do not have to remember to make their payment by the due date. Once initially setup, a recurring payment will happen until the customer revokes or cancels the authorization. Recurring payments provide corporates/businesses with more reliable expectations of funds availability. Typically, businesses will have fewer collection costs by using ACH compared to other payment methods. Types of recurring debit payments are: monthly utilities, i.e., water, gas, phone, monthly gym membership, insurance premiums, etc.

**Same Day ACH:** Same Day ACH credit and debit entries are available, which allows ACH Originators the option to send ACH entries and the Receiver to receive the entry on the same day. Same Day ACH is cheaper and settlement may be quicker than other payment channels. Institutions often use Same Day ACH for emergency payroll files, business-to-business payments, expedited bill payments, return processing, and account-to-account transfers.

**Third-Party Senders – They Are Not to be Feared!** A Third-Party Sender (TPS) acts as an intermediary between a company originating an ACH payment and an ODFI. Third-Party Senders and their ODFIs do have additional responsibilities within the network. Third-Party Sender relationships may provide income opportunities through high deposit balances and possible transaction fees. Third-Party Senders typically process transactions of high volume and low dollar amounts and risk can be mitigated; by performing proper due diligence, implementing strong internal controls, and knowing your financial institution's risk tolerance level.

**Transaction Security:** ACH debit and credit transactions are less susceptible to fraud compared to checks, wire transfers, and debit/credit card transactions. ACH is safer for merchants, consumers, and financial institutions. With adequate controls, ACH transactions can minimize financial losses due to human error.



## Marketing ACH For Your Institution

One of the most important decisions your institution will make is choosing a sales and marketing strategy for the organization and its ACH direction. The marketing strategy is different for each institution and can help unite the business vision and the objectives set forth in the ACH program.

Below are some key steps to consider when developing a comprehensive ACH Marketing Strategy:

- Obtain senior management's support
- Form an internal task force
- Establish an ACH marketing and sales team
- Develop a prospects list
- Evaluate prospects and analyze needs
- Prioritize prospects
- Prepare a business case, weighing the cost and risk of implementing ACH origination

## Payment Risk Considerations and Suggested Internal Controls

While the ACH Network is not without risk, the majority of payment fraud continues to be within other payment channels. Each financial institution's risk is dependent on the complexity of the services they offer. The good news is the risk can be mitigated with strong internal controls and a strong onboarding program including a healthy Know Your Customer (KYC) environment. KYC is a critical component of ACH risk mitigation.

**Credit Risk:** The risk that a party to a payment transaction will be unable to provide the necessary funds for settlement of the processing. For an ODFI to mitigate risk, the ODFI should implement underwriting standards, analysis of creditworthiness, and set appropriate exposure limits. Credit risk is mitigated by having strong internal controls, reasonable ACH exposure limits, documented onboarding and due diligence processes, and implementation of "true" prefunding.

**Compliance Risk:** For ACH activity, whether it is originated or received, the institution's compliance program should include Regulations CC, D, E, GG, BSA/AML, OFAC, *NACHA Operating Rules* and Uniform Commercial Code Article 4A (UCC 4A) for commercial payments. Compliance risk occurs when an institution does not comply with rules and regulations. Compliance risk is mitigated by ensuring staff receives adequate training.

**Cross-Channel Transaction Risk:** Cross-channel risk is the risk associated with the movement of fraudulent or illegal payment transactions from one payments channel to another (i.e., check or wire transfer to ACH). This risk is mitigated by monitoring transactions across multiple payment channels

**Fraud Risk:** In any electronic payment method, there is the risk of fraud, either by an external or internal party. With proper internal controls, including segregation of duties and dual control, a financial institution and its Originators can mitigate the risk of fraud.

**Operational Risk:** Operational risk occurs when a transaction is altered or delayed due to an unintentional error. This risk can be mitigated by having strong internal controls including a business continuity/disaster recovery plan, documented policies and procedures, and most importantly having educated staff on rules and regulations.



**Reputation Risk:** Reputation risk is the risk of adverse publicity and the possible resulting loss of confidence or business from an incident, event, or problem with the system.

**Systemic Risk:** Systemic risk is the risk posed to the reliability and soundness of the payment system as a whole. The ACH Operators have established risk management procedures to minimize the possibility of systemic financial institution failures associated with ACH settlement.

## How Can PaymentsFirst Assist?

### Consulting and Support Documents for ODFIs

PaymentsFirst provides consulting services to assist with developing ACH Origination processes such as documenting internal controls and development of policies and procedures. PaymentsFirst can provide forms, documents, and agreements that can get you get started in your ACH origination process. Some of these resources are available to members at no cost and some enhanced resources are sold at membership discount pricing. Developing and gathering all the necessary forms, documents, and agreements can be intimidating when starting a new program. PaymentsFirst can help your institution identify and understand the documents which may be needed for a rewarding ACH origination program. The following documents and forms are available for an ODFIs ACH origination program:

- 📄 ODFI/Originator/Third-Party Sender Agreements
- 📄 Third-Party Sender/Originator Agreement
- 📄 Debit and Credit Authorization Language
- 📄 Originator/Third-Party Sender Responsibilities
- 📄 ACH Origination Annual Review Form
- 📄 ACH Origination Application
- 📄 ACH Originator/Third-Party Sender Education
- 📄 Indemnification to Security Procedures
- 📄 Addendum to Agreement for Special SEC Codes
- 📄 Tri-Party Third-Party Service Provider, Originator, and ODFI Agreement
- 📄 Third-Party Sender Addendum to Master Services Agreement
- 📄 Third-Party Sender Client List Layout
- 📄 Third-Party Sender Audit and Risk Assessment Guides
- 📄 ACH Program Profitability Calculator

### Exhibit A - Profitability

We have created a profitability template to help institutions evaluate whether a proposed ACH relationship will be profitable. The template below can be provided at your request for evaluating profitability for each ACH relationship. Your institution may wish to include other data and factors when assessing the relationship. The fees and interest rates are only to portray the functionality of the template. PaymentsFirst does not provide pricing information to our members. We cannot discuss other institutions' prices or suggest a fee schedule for your institution.

Financial Institution Name					
ACH Program Total Profitability					
Number of Originators	a		Date:	January 1, 2019	
Department	ACH Department				
Originators' Avg Balances (All Accounts)			Net Interest Margin	0.00%	
<b>Income</b>			<b>Expenses</b>		
Earning Asset Rate			Cost of Funds		
Annual Int Income	A	\$0.00	Annual Int Expense	D	\$0.00
Monthly Fee Per Originator	b		Expense/Originator	e	
Number of Months	c		Number of Months	f	
Fee Income	B	\$0.00	Annual Orig Expense	E	\$0.00
Gross Income	C	\$0.00	Annual Expense	F	\$0.00
(A + B = C)			(D + E = F)		
(B = a*b*c)			(E = a*e*f)		
		ACH Net Income (Annual)			\$0.00

\*The above image is a profitability analysis for the ACH Department based on the number of Originators you have, the average account balances, fees assessed, and expenses. All fields in grey are fillable, while the other cells are protected. We can provide the template at your request.

Financial Institution Name						
ACH Origination Profitability Analysis						
<b>Originator:</b>					<b>Date:</b>	
<b>Officer:</b>						
<b>Average Balance (Annual)</b>					<b>Net Interest Margin</b>	0.00%
<b>Income</b>			<b>Expenses</b>			
<b>Earning Asset Rate</b>					<b>Cost of Funds</b>	
<b>Annual Int Income</b>	A	\$0.00		<b>Annual Int Expense</b>	D	\$0.00
<b>Monthly Fees</b>					<b>Expense/Originator</b>	
<b>Number of Months</b>					<b>Number of Months</b>	
<b>Fee Income</b>	B	\$0.00		<b>Annual Orig Expense</b>	E	\$0.00
<b>Gross Income</b>	C	\$0.00		<b>Annual Expense</b>	F	\$0.00
(A + B = C)			(D + E = F)			
<b>Relationship Profit/Loss</b>					\$0.00	

*\*\*The above image is a profitability analysis for an individual Originator. All fields in grey are fillable, while the other cells are protected. We can provide the template at your request.*