Key Components of an ODFI

Mini Deck

Disclosure

- ©2017 PaymentsFirst. All rights reserved.
- This material is not intended to provide any warranties or legal advice, and is intended for educational purposes only.
- NACHA owns the copyright for the *NACHA Operating Rules & Guidelines.*

2

1

Anti Trust Laws

NACHA DIRECT MEMBER
Regional Payments Associations℠

PaymentsFirst
Service · Education · Support

- PaymentsFirst is a not-for-profit organization and we closely adhere to all applicable laws and regulations.
- In accordance with Anti-Trust laws, we may not play any role in competitive decisions of members or their employees.
- During discussions with competitors and within the presentation materials we will and we ask participants to refrain from any discussion regarding pricing of products and services.

3

Important Info

PaymentsFirst
Service · Education · Support

Regional Payments Associations, through their Direct Membership in NACHA, are specially recognized and licensed providers of ACH education, publications and support. Regional Payments Associations are directly engaged in the NACHA rulemaking process and Accredited ACH Professional (AAP) program.

NACHA owns the copyright for the *NACHA Operating Rules & Guidelines*. The Accredited ACH Professional (AAP) is a service mark of NACHA.

DISCLAIMER:

- This presentation and applicable materials are intended for general education purposes and nothing in this presentation should be considered to be legal, accounting or tax advice.

- You should contact your own attorney, accountant or tax professional with any specific questions you might have related to this presentation that are of a legal, accounting or tax nature.

4

Agenda

- ACH Network Participants (including Third-Parties)
- Legal Framework
- General Rights and Responsibilities
- ACH Agreements and Risk Management
- ODFI Warranties
- Authorization Requirements
- SEC Codes
- Operations

5

ACH Participants

- Receiver
  - The receiving company, employee, organization, trading partner or consumer
- Receiving Depository Financial Institution
  - RDFI
- Originator
  - The originating company or individual
- Originating Depository Financial Institution
  - ODFI
- ACH Operator
  - Federal Reserve Bank (FRB)
  - Electronic Payments Network (EPN)

6

ACH Participants

ODFI ACH Operator RDFI

Originator

Receiver

7

Third-Party Service Providers

Key Components of an ODFI

8

Third-Party Service Providers

- An Organization that performs any function on behalf of the Originator, ODFI or RDFI
  - Related to processing of Entries
  - Creation of the Files or
  - Acting as a Sending Point or Receiving Point
 - An Organization acting as a Third-Party also is a Third-Party Service Provider

9

Third-Party Service Provider

Providing a Services to the Originator

Originator   ODFI   ACH Operator

Optional Agreement

Third-Party Service Provider   Processing   Agreements

10

Third-Party Service Provider

- Providing a Services to the ODFI

Originator

Third-Party Service Provider

ACH Operator

ODFI

Processing
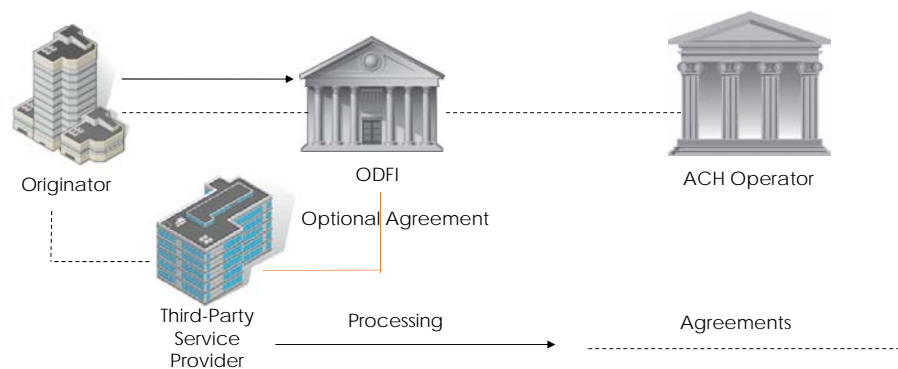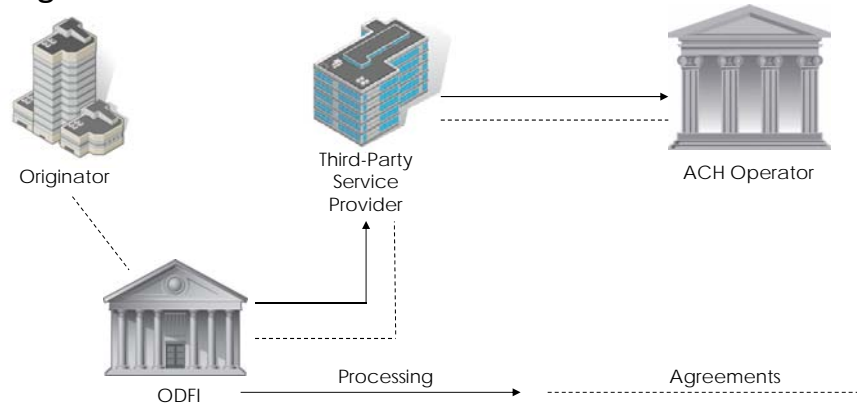
Agreements

Third-Party Sender

- Subset of a Third-Party Service Provider
  - Acts as intermediary between ODFI and Originator where no contractual agreement exists between the ODFI and Originator
  - TPS utilizes ODFI's routing number and settlement account

Third-Party Sender

Originator

ODFI

ACH Operator

Third-Party
Sender

Processing   Agreements
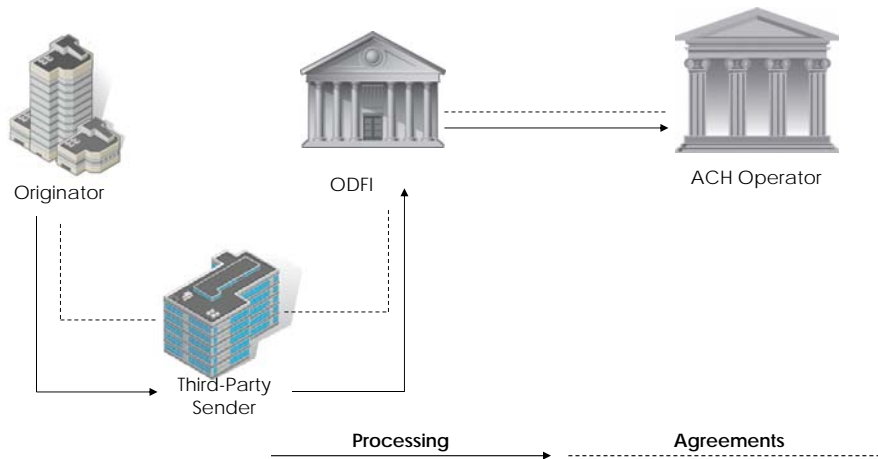
13

Legal Framework

Uniform Commercial Code 4A

- Governs commercial/wholesale credit Entries
- Comprehensive body of state law
- Choice of Law
  - Governed by the laws of New York unless superseded by agreement
- Some provisions may be altered through agreements while others cannot

14

Legal Framework

Uniform Commercial Code 4A Disclosures

- Entry may be transmitted through ACH

- Rights and obligations of the Originator are governed by the state laws of New York
  - Unless a different state is agreed upon by ODFI/Originator

- Credit given by RDFI to Receiver is provisional until final Settlement
  - Settlement not received, RDFI is entitled to a refund and Originator is not considered to have paid

15

General Rights and Responsibilities

- ODFI Verification of Originator, Third-Party Sender Identity
  - ODFI uses commercial reasonable method
  - Verification of identity
  - When entering Origination Agreement

- Termination, Suspension, and Audit of Originators and TPS
  - Default termination is 10-banking days notice by ODFI
  - Amended by ODFI/Originator Agreement

16

General Rights and Responsibilities

- Risk Assessments
  - Conduct assessment of ACH risk activity
  - Implement risk management program
  - Comply with regulator requirements

- Security Requirements
  - Non-consumer Originator, ODFI, RDFI, Third-Party Service Provider
    - Establish, implement, update polices & procedures
    - Protected Information
      - Protect confidentiality & integrity
      - Protect against threats to security
      - Protect against unauthorized use

17

General Rights and Responsibilities

An ODFI is responsible for all Entries originated through the ODFI including

- Originator
- Third-Party Sender
- Direct Access

- An ODFI is responsible for its Originators and Third-Party Senders compliance with the Rules

18

ACH Agreements

- ODFI Agreements at a minimum include
  - a) Must authorize the Originating Depository Financial Institution to originate Entries to the Receiver's account(s)
  - b) Must agree to be bound by the *NACHA Operating Rules*
  - c) Must agree not to originate any Entries that violate the laws of the United States
  - d) Restrictions on the types of ACH Entries to be originated

ACH Agreements

- ODFI Agreements at a minimum include (Continued)

  - e) The right of the ODFI to terminate or suspend the agreement for breach of the rules
  - f) The right of the ODFI to audit the Originator's, Third-Party Sender and its Originator's compliance to the rules
  - g) Third-Party Sender (exclusively) will enter into an Agreement with each of its Originators
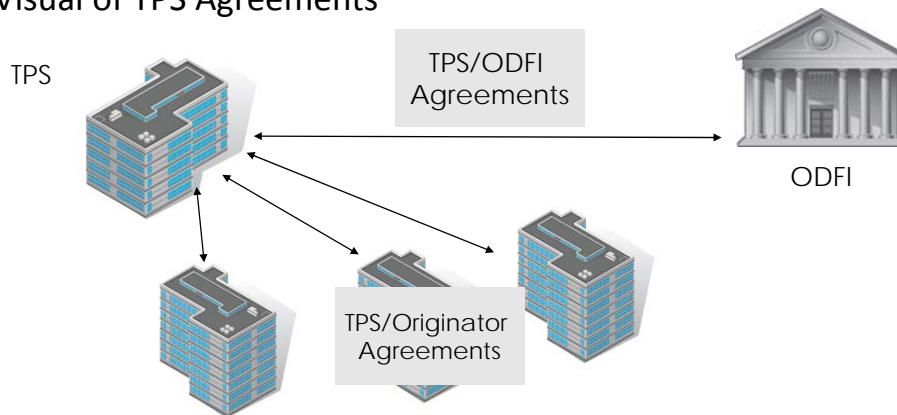
ACH Agreements

- Visual of Origination Agreements

Originator — Co/ODFI Agreements — ODFI

ACH Agreements

- Visual of TPS Agreements

TPS — TPS/ODFI Agreements — ODFI

TPS/Originator Agreements

Risk Management

ODFI Risk Management

- Due Diligence includes
  - Reasonable belief that Originator or Third-Party Sender has the capacity to perform obligations according to the NACHA Operating Rules
  - Assess nature and risk of Originator's or Third-Party Sender's activity
  - Establish, periodically review, and enforce exposure limits
  - Monitor origination and return activity across multiple Settlement Dates
  - Enforce Origination agreement restrictions

ODFI Warranties

ODFI warrants to each RDFI and ACH Operator that:

- Entry is properly authorized
- Origination agreement not terminated
- Originator has no knowledge of revocation by Receiver
- Originator has no knowledge of termination of Receiver account agreement with RDFI
- Authorization not terminated in whole or part by operation of law

ODFI Warranties

ODFI warrants to each RDFI and ACH Operator that: (continued)

- Entry contains required information
  - Correct account number
  - Necessary information for posting
- Credit Entry is timely
- Debit Entry satisfies an obligation, corrects an error or reclaims an amount received after death or legal incapacity
- Secure transmission of banking information
- ODFI has verified identity of Originator, TPS

25

Authorization Requirements

Key Components of an ODFI

26

Authorization Requirements

An authorization must

- Be readily identifiable as an authorization
- Have clear and readily understandable terms
  - Including amount, timing of debits
- Provide that the Receiver may revoke the authorization only by notifying the Originator in the manner specified in the authorization
  - For a single entry scheduled in advance, any such revocation right shall afford the Originator a reasonable opportunity to act

27

Authorization Requirements

- Credit Entries to Consumer Account
  - Not required to be in writing
  - If both Originator and Receiver are natural persons no authorization by Receiver is required and no warranty is made by ODFI

- Debit Entries to Consumer Account
  - Must be in writing and signed or similarly authenticated
    - Except for specific types of Entries (notice)
    - Originator must provide each Receiver with an electronic or hard copy of the authorization

28

14

Authorization Requirements

- Notice of variable debits to Consumer Account
  - Change in Amount
    - Originator must provide Receiver written notice 10 calendar days prior to scheduled Entry to be initiated

  - Change in Date
    - Originator must provide Receiver written notice seven calendar days prior to scheduled Entry to be debited

  - No Notice Required for Change of Amount within agreed range

29

Authorization Requirements

Non-Consumer Account

- Credit or Debit Entries to Non-Consumer Account
- An agreement in place between two companies doing business together
- Originator must obtain the Receiver's agreement to be bound by these Rules

30

Authorization Requirements

Request for Copy of Authorization

- Originator
  - Must maintain original or copy of authorization for two (2) years from termination or revocation
    - Originator must be able to make the copy of authorization available to the ODFI

- ODFI
  - Upon receipt of RDFI's written request
    - ODFI must provide within 10 Banking Days
    - ODFI may NOT charge for copy

31

Authorization Requirements

Authorization Requirements for Check Conversion Products

- Notice Language for ARC, BOC and POP
  - "When you provide a check as payment, you authorize us either to use information from your check to make a one-time electronic fund transfer from your account or to process the payment as a check transaction."

- Additional Language for BOC only
  - "For inquires, please call [Retailer phone number]"

- Additional authorization requirement for POP only
  - Written authorization (signed receipt)
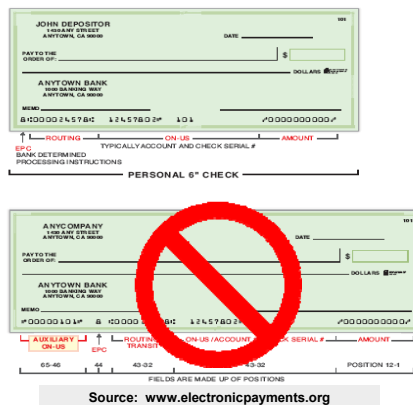
32

16

Authorization Requirements

Authorization Requirements

- Requirements for Eligible Source Documents
  - Must not contain an Auxiliary On-Us Field
  - Must be $25,000 or less
  - Pre-printed Check Serial Number
  - Routing number, account number, and Check Serial Number encoded in magnetic ink
  - Completed and signed (except for POP Entries)

Authorization Requirements

- Source Documents Example

Source: www.electronicpayments.org

Operations

Key Components of an ODFI

35

Operations

Effective Entry Date vs. Settlement Date

- Effective Entry Date
  - Date specified by the Originator on which it intends a batch of Entries to be settled

- Settlement Date
  - Date (a 3-digit Julian date) for a batch of Entries is inserted by the Receiving ACH Operator

36

Operations

Effective Entry Date vs. Settlement Date

- Credit Entries
  - The Effective Entry Date must be either one or two Banking Days following the Banking Day of processing by the ACH Operator

- Debit Entries
  - The Effective Entry Date must be one Banking Day following the processing date

37

Operations

- ODFI may Dishonor a Return (except IAT) if:
  - It can substantiate that the RDFI failed to meet the time deadlines for the return entry
  - The Return Entry contained incorrect or does not contain all information (unable to process)

- Time frame
  - ODFI must transmit within Five Banking Days after the Settlement Date of the Return Entry
  - Return Reason Codes
    - R61, R62, R67, R68, R69, & R70

38

Reinitiation

Reinitiation of Entry

- Originator or ODFI may Reinitiate any Entry, other than an RCK, that was previously returned for
  - R01 - Insufficient funds or R09 - Uncollected funds
    - Entry may be reinitiated no more than two times after return of original Entry
  - Entry returned for R08 - Stop Payment and Reinitiation is authorized by Receiver
  - Originator or ODFI remedies the reason for the Return
  - Must be reinitiated within 180 days after Settlement Date of original Entry

Reinitiation

Reinitiation of Entry

- An Originator or ODFI may Reinitiate an RCK Entry that was previously returned if
  - The RCK Entry has been returned for insufficient or uncollected funds; and
  - The item to which the RCK Entry relates has been presented no more than one time through the check collection system (as a Check, substitute check, or image) and no more than one time as an RCK Entry

Prenotification Entries

Non-Monetary Entry Transmitted by an Originator prior to the initiation of the first credit or debit Entry to a Receiver's account
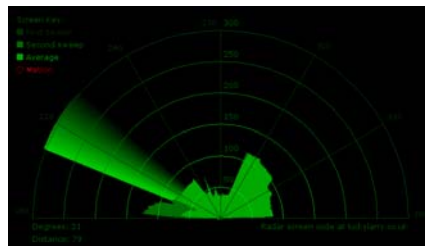
- Used to verify the Receiver's account number at the RDFI

- Optional for the Originator

- Originator and ODFI must comply with all rules and formatting requirements
- Must wait and allow at least three Banking Days from the Settlement Date of the Prenotification before a live dollar Entry may be transmitted

41

Prenotification Entries

If Prenote is Returned to the ODFI by opening of business the second Banking Day following the Settlement Date of the Prenote

- ODFI provides Return to the Originator

- Originator should research the problem according to the Return Reason Code

- Originator must remedy the reason for the Return prior to Transmitting a subsequent Entry

42

Prenotification Entries

- Reduction of Waiting Period

March						
Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
1	2 Prenote Sent (ODFI)	3 Prenote Settles (RDFI)	4 NOC Sent (RDFI)	5 ODFI Receives NOC	6 Originator may send live dollar Entry if correction made	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

43   43

Prenotification Entries

- Reduction of Waiting Period

March						
Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
1	2 Prenote Sent (ODFI)	3 Prenote Settles (RDFI)	4	5 NOC Sent (RDFI)	6 ODFI Receives NOC; Originator may send live dollar Entry	7
8	9	10 ODFI required to deliver NOC information to Originator	11	12	13	14
15	16	17	18 Originator must make correction	19	20	21
22	23	24	25	26	27	28
29	30	31				

44

Reversals

Reversing File

- Initiated by an Originator or an ODFI to reverse each Entry within a duplicate or Erroneous File

- Must be Transmitted within five Banking Days after the Settlement Date of the duplicate or Erroneous File
  - Transmit within 24 hours of discovering error

- ODFIs may not reverse Files in the case of failed settlement by the Originator

45

Reversals

Reversing File

- "REVERSAL" must be specified in the Company Entry Description Field within the Company/Batch Header Record

- A Correcting File is required to accompany Reversing File when File is reversed because of an Erroneous File
  - Unless the Erroneous File was a duplicate

46

Reversals

Reversing File

- ODFI or ACH Operator that initiates Reversing or Correcting File indemnifies other Participating DFIs and ACH Operator from losses
  - ODFI is responsible for Reversing or Correcting Files initiated by its Originators

47

Reversals

Reversing Entry

- Initiated by an Originator to correct Erroneous Entry

- Must be Transmitted within five Banking Days after the Settlement Date of the Erroneous Entry

- ODFI indemnifies every Participating DFI and ACH Operator

- Originator must make a reasonable attempt to notify the Receiver of the Reversing Entry

48

Letter of Indemnity

ODFI Request for Return

- ODFI may contact the RDFI and request the return of a particular Entry
  - R06 – Returned per ODFI's Request
  - The RDFI is not obligated to, comply with request
  - If the RDFI agrees to comply the ODFI indemnifies the RDFI against any losses or liabilities which may result
  - Return time frame not defined, determined by ODFI and RDFI

49

50