Compliance Beyond the ACH Rules and Sound Practices for the ACH Audit

Jim Petkovits, AAP, NCP
Vice President; Education
WesPay

Sharing our passion for payments
Agenda

» ACH Audits and Risk Assessments
» Common Audit Findings
» Stop Payment Issues
» Authorization Revoked and Unauthorized
  • Regulation E Disputes vs. ACH Rules
» Reclamations
» Disclosure Requirements
ACH Audits and Risk Assessments
Audit & Risk Assessment Cycle

ACH Audit

- Annual requirement (subsection 1.2.2 of ACH Rules)
  - Deadline is Dec. 31st, but you may have own 12 month cycle
  - New ACH rules go into effect March & September
- Who is required? All participating DFIs and Third Party Senders
- Scope? “Accordance with Appendix 8” or “all provisions of the NACHA Operating Rules?”
- Who performs? Internal, outside, or independent auditor
Audit & Risk Assessment Cycle

» ACH Risk Assessment
  • Not Time Driven – A participating DFI must “conduct, or have conducted, an assessment of the risks of its ACH activities and implement, or have implemented, a risk management program on the basis of such assessment.”

» When to update?
  • Advice: at least annually or changes/expansion to ACH services, policies, procedures, or rules
Audit & Risk Assessment Cycle

» Related functions to consider:
  o OFAC BSA/AML Compliance
  o Business Continuity
  o ACH Risk Management
  o Federal Govt. Payments
  o IT

» Integrate ACH into these audits/reviews!
Common Audit Findings
8.2.a/b Records/Electronic Records

» Verify that records of entries originated and received and sent are retained for six years
  • This includes returns and NOCs

» Verify information relating to the entry stored electronically may be reproduced for the account holder or other financial institution that originated, received or transmitted the entry

» The common finding here is that while records have been retained they are no longer in a format available to the financial institution
8.3.b Notification of Change

» Verify that Notifications of Change are transmitted within two banking days of settlement of entry to which the NOC relates

• Exceptions - NOC due to acquisition or merger

» Technically not a “finding” but the common issue is the policy behind NOCs. If a financial institution is originating too many NOCs they may be placing themselves in unnecessary risk
8.3.e Statements

» Verify that consumer statements contain all required information
  • For **POS**, Terminal ID Code and/or Terminal City and State
  • For **IAT**, the Originator Name

» The common finding here is that the proper information for these two SEC Codes is not properly placed on the consumer statement. Unlike other SEC Codes this information is taken from the addenda records for these SEC Codes
8.3.j Written Statement

» Review records and procedures to ensure ‘Written Statements’ are received for all R05, R07, R10, R37, R51 and R53 returns, and that returns are available to the ODFI by the 61st day following settlement

» The common finding here relates to the use of the wrong Return Reason Code, for example R08 instead of R07 or a CCD returned R10 that should have been returned R05 or was untimely

• 8.3.i Stop Payments
8.3.1 EDI Records

» Review records and procedures to ensure that, when requested, corporate receivers are provided all payment related information within two banking days for all CCD, CTX, CIE and IAT entries

» For Health Care EFT ensure a secure method of delivery is available

» The common audit finding here is how is this information provided? If the EDI record is e-mailed ensure proper encryption is used
  • 8.2.d Data Encryption
8.4.c ODFI Risk Management

» ODFI must perform due diligence to form a reasonable belief that the Originator or Third Party Sender has the capacity to perform its obligations in conformance with the Rules
  • Assess the nature of the Originator’s or Third Party Sender’s ACH activity and the risk it presents
  • Establish, implement, *periodically review* and enforce exposure limits
  • Monitor origination and return activity over multiple settlement dates
  • Enforce restrictions on types of entries originated

» *The common finding here relates to overall Originator Risk Management*, how often are risk limits reviewed, how are return rates monitored and reported, how are restrictions of SEC Codes enforced and over limit files suspended
8.4.e NOCs

» Review internal procedures to determine that information related to Notifications of Change (NOCs) and Corrected NOCs is provided to Originator within two banking days of receipt

» **Not technically a “finding”, but The Originators failure to respond to the NOC certainly is a Rules violation.** . The ODFI warrants that the change will be made within 6 days or prior to the next transaction
8.4.j Reversing Files & Entries

» Verify that Reversing files & entries are originated in accordance with the requirements of these rules.

» The common finding here is that the Entry Description “REVERSAL” is not used. This is particularly important considering a 2015 Rules Change
8.4.m Registered Direct Access Relationship

» Verify the ODFI has registered its direct access status with NACHA

» And if direct access relationships exist the ODFI has Board approval and is able to communicate statistical reporting to NACHA

» The common finding here is that while direct access is rare and most financial institutions registered back in 2010 the confirmation may have been lost
8.4.n Education of Originators

» Verify that the ODFI has kept Originators and Third Party Senders informed of their obligations under these rules.

» The issue here is how are Originators educated on their requirements for proper Data Security related to the ACH Files they send and the authorizations they obtain
  • 8.2.g Security Policies and Procedures
Stop Payment issues
When it was easy..
“Stop Payment”

» Consumer wishes to stop only one specific debit
» Does not revoke all future debits from the payee/originator
» Examples:
  • Disputes in billing amount on a recurring ACH transaction (utility bills, etc.)
  • Receipt of faulty merchandise
  • Prevent duplicate payment in case of last loan payment
ACH Stop Payment: Documentation Considerations

» Transaction information

» Consumer notice requirements:
  • Three banking days….when?
  • Consumer liability to provide correct information
  • “Reasonable opportunity”….when?

» Possible consumer responses:
  • Stop all future payments indefinitely
  • Stop the next payment only
  • Stop a series of payments
NACHA “Stop Payment” Provisions

- Consumer may stop payment of a debit entry
- Three banking days notice provided to RDFI either verbally or in writing
- RDFI may honor a stop payment request within the three banking day time frame/no resultant liability
- RDFI may require written confirmation of an oral stop payment order within 14 days of that order, provided the RDFI notifies Receiver of the requirement/address to send the confirmation to at time of oral order
NACHA “Stop Payment” Provisions

- ARC, BOC, POP, RCK or Single Entry IAT, PPD, TEL or WEB: stop payment order must be placed to allow the RDFI a “reasonable opportunity” to act on the request.

- Language is different because these type of stops are for non-recurring transactions; difficult to require a three-banking day lead-time when purchases are often spontaneous.

- Special return codes.
Special Stop Payment Return Codes for “E-Check” Transactions

- **R38**—Stop Payment on Source Document (ARC, BOC)
  - RDFI determines that a stop has been placed on the source document to which the ARC entry relates
  - Returned within 60 days of entry settlement date
  - No WSUD required

- **R52**—Stop Payment on Item (RCK)
  - RDFI determines that a stop has been placed on the item to which the RCK entry relates
  - Returned within 60 days of entry settlement date
  - No WSUD required
NACHA Stop Payment Order: Duration

- A stop payment order will remain in effect:
  - 1) for an indefinite timeframe;
  - 2) until payment of the debit entry has been stopped; or
  - 3) until the Receiver withdraws the stop payment order, whichever occurs earliest.
Stop Payments Affecting Non-Consumer Accounts

- RDFI may require a “reasonable opportunity” to act on the request
- Verbal stop payment orders must be confirmed in writing within 14 days
- Not affected by any provisions or Regulation E
- Effective until whichever happens first:
  - Return of debit Entry
  - Withdrawal of stop notice
  - 6 months, unless renewed in writing
Authorization Revoked and Unauthorized
Revoked Authorization

- Consumer admits relationship with Originator
- Consumer has contacted Originator to revoke authorization according to terms of the authorization agreement (NACHA Rules require)
- Consumer completes required documentation (WSUD)
- Only to be used with PPD, TEL and WEB
Revoked Authorization: Return Time Frame

» RDFI may transmit a return (R07) to its ACH Operator by its deposit deadline for the adjustment entry to be made available to the ODFI no later than the opening of business on the banking day following the sixtieth calendar day following the Settlement Date of the original entry.

» Disputed entries beyond the “60 day” timeframe:
  • RDFI has no further obligation to account holder
  • Customer service: may want to contact ODFI and ask that they accept a late return
Unauthorized Returns

» R10 (or R51) - Unauthorized - (Consumer SEC Only, Not CCD or CTX (R05 ))
  • 60 days from Settlement
  • WSUD

» Consumer did not authorize the debit either in writing, verbally or electronically with the Originator

» Improper Item (POP/ARC/BOC/RCK transactions only)

» Authorized different amount or earlier date

» 60 day ACH Return Vs. 60 day Regulation E Dispute
  • What can the RDFI do?
WSUD Form

Signature:
- Must confirm status as “authorized signer” on account
- Debit not originated with fraudulent intent
- Attest to the accuracy and truth of the statement
WSUD Requirements

» Need not be signed “in person”
» May be provided by FAX or other electronic means
» Can be used for more than one “unauthorized debit” from the same Originator
» Must be signed and dated on or after the Settlement Date of the entry/entries
» Authentication of the Customer is the liability of the RDFI
» RDFI Indemnity
WSUD Requirements

» Copy of WSUD may be requested by ODFI within one year of the date of initiation of the adjustment (return) entry

» RDFI must produce a copy within 10 days of the date on which it receives the ODFI’s request

» WSUD is the minimum requirement under the NACHA Rules; RDFI may choose, at its discretion, to obtain an affidavit from its account holder

» Under NACHA rules, a WSUD is not required to be notarized
Reg E “Errors”

Definition of Error:

- An unauthorized electronic fund transfer
- An incorrect electronic fund transfer to or from the consumer’s account
- The omission of an electronic fund transfer from a periodic statement
- A computational or bookkeeping error made by the FI
- Consumer’s receipt of an incorrect amount of money from an electronic terminal
“Notice to financial institution is given when a consumer takes steps reasonably necessary to provide the financial institution with the pertinent information, whether or not a particular employee or agent of the institution actually receives the information.”

- Can be given in person, on phone or in writing
- If in writing, is considered to have given notice at the time it is deposited in the mail
Definition of Error

» Unauthorized electronic fund transfer
» Incorrect EFT to or from a consumer’s account
» Omission from a periodic statement of an EFT to or from a consumer’s account that should have been included
» Computational or bookkeeping error by the financial institution relating to an EFT
Definition of Error (continued)

» Consumer’s receipt of an incorrect amount of money from an electronic terminal

» An EFT not identified in accordance with the requirements of Reg E

» A consumer’s request for any documentation required to be provided the consumer or additional information or clarification concerning an EFT
NACHA Rules vs. Regulation E Concerning Errors

» NACHA rules related to the Written Statement of Unauthorized Debit

» Regulation E requirements related to error investigation documentation
  • Qualification and retention

» Regulation E requirements related to notices to consumer following error investigation
Notification of Error From Consumer

» Oral or written notice
  • Must be received no later than 60 days
    o After first statement sent which reflects error
    o After additional information sent as requested by consumer
  • Must identify consumer’s name and account number
  • Must indicate the consumer’s belief that and reasons why an error exists in account
  • Must indicate, to the extent possible, the type, date and amount of the error
Financial Institution’s Responsibility

» May require written confirmation to be received within ten business days of an oral notice
  • If the consumer is advised at time of oral notice and is provided address
Investigation of Errors

» Promptly investigate to determine if error occurred
» Send results within ten business days
» Take up to 45 calendar days to investigate with certain restrictions
  • Provisionally credit amount of alleged error
  • Provide proper notice to consumer within two business days about the amount and date of recrediting indicating full use of funds pending determination of error
  • Allow consumer full use of provisional funds
  • Give notice of debiting of funds if no error occurred and honor certain items
Extension of Time Periods

» 20 days instead of 10 days if:
  • Notice of error involves electronic funds transfer to or from new account

» 90 days instead of 45 days if:
  • Notice of error involves electronic funds transfer to or from new account
  • Item was “not initiated within a state”
  • Resulted from a point of sale (POS) debit card transaction
Investigation Finds Error

- Correct the error within one day
- Report the results to the consumer within three business days after completing the investigation
- Make provisional credit final if 45 day timeframe was used for the investigation
Investigation Finds No Error

» Mail or deliver to the consumer a written explanation of the findings within three business days after concluding investigation

» Provide copies of documents used in making its determination if requested by consumer

» Debit the provisionally credited amount from the consumer
Unauthorized Returns – Regulation E

» Financial Institution Reimbursement

• Reg E does not address ability of FI to seek reimbursement for unauthorized transfers, once consumer’s account has been credited. FI must rely upon its own ability to proceed against the unauthorized user under applicable law, or if the transaction was processed through an electronic funds transfer network, by the rules of the network.
Reclamations – Private Sector vs. Federal
Reclamations

NACHA Operating Rules allow reclamations for pension, annuity, or other benefit payment if Receiver is deceased and neither Receiver’s estate or any other account-holder is entitled to the payment.

Reclamation Entry should include:

- Name and account number of deceased
- Dollar amount equal to or less than amount of pension, annuity, or benefit payment
- Approximate date the entry being reclaimed was initiated
- “RECLAIM” in Company Entry Description Field of Batch Header Record
Reclamations

**Time Limitations**

- Originated or written demand for payment sent within 5 banking days after Originator receives notice of death of Receiver

- If returned by RDFI, Originator may make written demand for payment within 15 banking days after it receives return
Reclamations

» RDFI Liability
  • Limited to lesser of:
    o Amount of payments the Receiver was not entitled to or
    o Amount in the Receiver’s account at the time it received reclamation or written demand and has had a reasonable opportunity to act
Reclamations

» Alteration by Agreement

• RDFI and Originator may agree to alter, amend, or supersede liability provisions of NACHA Rules by written agreement

• Agreement must stat that it is a master agreement applicable to all pensions, annuity, or other benefit payments sent by Originator to the RDFI for the benefit of all Receivers having accounts at the RDFI

• REMEMBER: All master agreements are subordinate to claims or demands of the U.S. Government under 31 CFR 210 (Green Book). Originator must reimburse RDFI for any payments made to Originator that are subsequently claimed by U.S. Government
Payments Subject to Reclamations

» Social Security benefit & disability (SSA)
» Supplemental Security Income (SSI)
» Black Lung disability (Dept. of Labor)
» Military and Coast Guard retirement (DFAS)
» Civil Service annuity (OPM)
» Veterans benefits (VA)
» Railroad retirement annuity (RRB)
» Central Intelligence Agency annuity (CIA)
» Workman’s compensation (FECA)
» Longshoremen’s and Harbor workers
» Compensation Act (Dept. of Labor)
» Any other Federal retirement or annuity
Payments Not Subject to Reclamations

» Federal salary, allotments and travel payments
» U.S. Savings bond payments
» Vendor/Miscellaneous payments
» IRS tax refunds
» Discretionary allotments
» Public Debt payments (TreasuryDirect)
» Misc. payments, i.e. grants, loans, fees, etc.
Federal Government Reclamations

» 120 day rule
  • Reclamations should be sent within 120 days of the agency discovering the death of the beneficiary

» 60 day rule
  • Financial Institutions must respond to all reclamations within 60 days to limit their liability
Reclamation Resolutions

3 possible solutions

• Return the entire amount of the reclamation from the account

• Return reclamation with proof of prior return of requested entries

• If the balance of the account is less than the reclamation, return the balance within 60 days to limit your liability (check balance within 24 hours of reclamation receipt)
  
  o If returning less than the full amount, FED account may also be debited the 45 day amount
  
  o If 60 day deadline is missed FED account will be debited the full amount of the reclamation
Actual and Constructive Knowledge of Death

Used to determine F.I. Liability after the date of death

• Actual knowledge through:
  o DNE *A DNE from one agency is like a DNE from all agencies*
  o Executor of an estate
  o Family member reporting death
  o Funeral home or other group reporting death

• Constructive knowledge through:
  o Unopened letter at RDFI (example)

• Death of recipient after end of month before payment posts

https://secure.ssa.gov/apps10/poms.nsf/lnx/0202408650
Errors in Death

If the person did not die you can terminate the reclamation with proof

- Drivers license
- A signed, dated, and notarized statement
- A written statement from the authorizing Federal Agency
Disclosures
Disclosure Requirements

» UCC 4A Language
» Reg E Language
» Stop Payment Language
» OFAC Language
» Other Disclosures
Disclosures – NACHA Rules

» Notice Required by Originator for Variable Debits
  • Change in Amount (10 days before)
  • Receiver’s Election for notification of change in amount range
  • Change in Date (7 days before)
Disclosures – UCC 4A

» **ODFI** required to provide to **Originators**:  
  - Entry may be Transmitted through the ACH Network  
  - Choice of Law  
    - NACHA default is NY; should specify home state  
  - Provisionality of Payment – not final until RDFI received final settlement through Federal Reserve Bank  
  - If RDFI entitled to refund from Receiver if payment not received for entry, Originator will not be considered to have paid Receiver
Disclosures – UCC 4A

» RDFI required to provide to Receivers:
  • Entry may be Transmitted through the ACH Network
  • Choice of Law
    o NACHA default is NY; should specify home state
  • Provisionality of Payment – not final until RDFI received final settlement through Federal Reserve Bank
  • If RDFI entitled to refund from Receiver if payment not received for entry, Originator will not be considered to have paid Receiver
  • RDFI not required to provide notice to Receiver of receipt of entry unless RDFI agreed to do so
Disclosures - Stop Payments

» Stop Payments Notification Timeframe

• Consumer Accounts:
  o Recurring ACH Entries – Receiver required to provide 3 day notice
  o Single ACH Entries – “Reasonable Opportunity”

• Non-Consumer Accounts:
  o “Reasonable Opportunity”
Disclosures – Stop Payments

Expiration Conditions

- Consumer Accounts:
  - Withdrawal of order
  - Return of the entry/entries

- Non-Consumer Accounts:
  - Withdrawal of order
  - Return of the entry/entries
  - Six months from the date of the stop payment order, unless renewed in writing
Disclosures - Dispute Timeframes

» Do you separate consumer account vs. non-consumer agreements, or do you combine them?

• If combined, what dispute timeframe do you quote?
  o Only Reg E? (60 days from statement)

  o What about Non-Consumer ACH return timeframes?
    - Non-Consumer ACH items have shorter window

• If you have a combined account agreement for consumer and non-consumer accounts, be sure to provide “next day” notification deadline for Non-Consumer accounts
Disclosures - OFAC

» Include possibility of delaying, freezing or not posting IAT entries due to OFAC requirements (both consumer and non-consumer accounts)
Disclosures – Reg E

» Reg E disclosure requirements
  • Initial terms and conditions
  • Changes in terms and conditions
  • Error resolution notices
  • Receipts at Electronic Terminals
  • Periodic statements

» Compliance Guidance
  • Include disclosure notices in legal agreements and annual T&C notification
  • Reg E model clauses: Appendix A to Part 1005
Other Disclosures

» **Regulation D**
  • Limit of six withdrawals or outgoing transfers per month from savings accounts.

» **Reg GG (non-consumer accounts)**
  • Unlawful internet gambling
Thank you!