

# ACH Origination Guide

## Facts & Originator Responsibilities

The ACH Network, which provides for the interbank clearing of electronic payments, is governed by *The NACHA Operating Rules and Guidelines (Rules)*. The *Rules* apply to all entries and entry data transmitted through the ACH Network. **As an ACH Originator, you must comply with and are bound by the *Rules*.** To ensure compliance, all ACH Originators must have access to a current copy of the *Rules*. The ACH Rules for Corporate Originators is published annually and may be ordered at [www.umacha.org](http://www.umacha.org) or accessed on-line at [www.achrulesonline.com](http://www.achrulesonline.com).

*North Star Bank (Bank)* provides this document as a brief summary of ACH facts and ACH Originator Responsibilities. It is not a replacement or substitution for the *Rules*, which are subject to change.

### **ACH Facts**

- ACH entries are categorized as “consumer” or “corporate.”
- ACH is capable of crediting or debiting checking or savings accounts.
- ACH entries are received by most financial institutions.
- ACH is a batch system (not real time).
- ACH entries are irrevocable once they have been sent for processing.
- ACH stop payments do not have an expiration date.

### **ACH Legal Framework**

You are required to abide by multiple rules and agreements including, but not limited to, the following when initiating

ACH transactions:

- NACHA Operating Rules ([www.nacha.org](http://www.nacha.org))
- Regulation E (for consumer entries)
- UCC4 (for corporate credits)
- *Bank Deposit Agreement and Terms and Conditions*
- *Bank Cash Management Agreement*
- Authorizations from employees, customers, etc.
- *Bank and Corporate agreements*

### **Definitions of ACH Participants**

**Originator** – The Originator is the entity or company that agrees to initiate ACH entries into the payment system according to an arrangement with a Receiver. The Originator is usually a company directing a transfer of funds to or from a consumer or another company’s account.

**Originating Depository Financial Institution (ODFI)** – The ODFI is the financial institution that receives the payment instructions from Originators and forwards the entries to the ACH Operator.

**Automated Clearing House Operator** – An ACH Operator is the central clearing facility operated by a private organization or the Federal Reserve Bank on behalf of Depository Financial Institutions.

**Receiving Depository Financial Institution (RDFI)** – The RDFI is the Depository Financial Institution that receives ACH entries from the ACH Operator and posts the entries to the accounts of its depositors (Receivers).

**Receiver** – A receiver is a natural person or an organization that 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.

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### How Does the ACH Network Function?

As the Originator, your company must first obtain authorization to initiate a transaction to the Receiver's account or provide notice to the Receiver that a transaction will be initiated to their account. Your company (Originator) then creates a file of ACH transactions assigning a company name that is easily recognized by the Receiver. The file is then sent to your Originating Depository Financial Institution (ODFI), North Star Bank.

The ODFI collects ACH files from Originator with which it has contractual relationships, verifies the validity of these files and at specified times, transmits these files to the ACH Operator. The ACH Operator receives ACH files from the ODFI, edits the file to make sure they are formatted properly and distributes files of entries to the Receiving Depository Financial Institution (RDFI). The RDFI receives files of entries from the ACH Operator for its account holders. Entries are posted based upon the Settlement Date and account Number. Periodic statements are provided to the Receiver with descriptive information about the ACH transaction, including the date of the transaction, dollar amount, payee (Originator) name, transaction description (i.e. payroll, rent,).

### How Are ACH Funds Settled?

Settlement is the actual transfer of funds between financial institutions to complete the payment instructions of an ACH entry. The Federal Reserve Bank provides settlement services for ACH entries. The timing of settlement is based upon the Effective Entry Date indicated on the ACH file and the time of its delivery to the ACH Operator. Your company as the Originator will determine the Effective Entry Date of the file you send to your ODFI. This is the date your company intends the entries to post to the accounts of the Receivers (employees or customers). When the ACH Operator processes an ACH file, the Effective Entry Date is read and entries are settled based upon that date, known as the Settlement Date. The Effective Entry Date in most cases is the same as the Settlement Date, but it is possible that the Settlement Date could be after the Effective Entry Date. For example, if the ACH Operator cannot settle on the Effective Entry Date due to untimely file delivery, a stale date, weekend or holiday, the ACH Operator will apply a Settlement Date of the next business day.

### Your Responsibilities as an Originator

- Obtain proper authorizations, dependent upon the transaction type, and retain authorizations for two years past revocation.
- If requested by the *Bank*, provide a copy of the authorization. The *Bank* may request to see your authorizations from time to time as part of an annual audit.
- Send entries on the proper date.
- Give appropriate notice to debtor if changing amount or date.
- Cease subsequent entries when notified.
- Make necessary changes to payee account information within three (3) banking days upon receipt of a Notice of Correction or before another entry is sent.
- Check payees against OFAC compliance checklists.
- Protect the banking information received to originate transactions.
- Ensure your computer and you are protected as outlined in the Cash Management Agreement.
- Ensure the Originator is clearly identified as the source of the ACH transaction. Specifically, populate the Company Name Field of the NACHA formatted file with a name known to and readily recognized by the Receiver of the entry.

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### **Direct Deposit Payroll Authorizations (Consumer)**

- Use a direct deposit authorization form that collects employee account information. This form should allow the company to make credit and debit entries in the event a payroll adjustment is necessary.
- Obtain a voided check from the employee (if possible).
- The most common SEC code for direct deposit is PPD.

### **Consumer Debit Authorizations**

- For consumers, an authorization to debit an account must be in writing or “similarly authenticated.”
- The most common SEC code for consumer debits is PPD.

### **Corporate Authorizations**

- For companies, there must be a record of an agreement between the two parties.
- The most common SEC codes for corporate transactions are CCD or CTX, depending upon addenda origination. It is used for debits and credits.

### **Changing Date or Amounts of Debits**

- ACH Rules require you to notify your debtors of any changes in date or amount debited under the following circumstances:
  1. Seven (7) calendar days notice for a change of date (consumer and corporate).
  2. Ten (10) calendar days notice for a change in amount (consumer only).
- Sending the notice via U.S. Mail is acceptable.

### **Prenotifications (Prenotes)**

- Prenotes are zero-dollar entries that precede the first live entry. The purpose of a prenote is to verify account information.
- Prenotes are optional for you to send. However, if sent, prenote rules must be followed and a prenote must precede the first live entry by at least three (3) banking days.
- The Receiving Bank is not required to validate the name of the payee on the prenote, although many do; they are only required to check the account number.

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### Notice of Change (NOC)

- NOC is created by the Receiver's financial institution to notify the originator (via the *Bank*) that:
  1. Previously valid information in an ACH entry (Direct Deposit/Direct Payment) is now outdated, and needs to be **changed**.
  2. Information in an ACH entry (Direct Deposit/Direct Payment) is erroneous, and needs to be **corrected**.
- The *Bank* will notify you of any NOCs received on your behalf.
- ACH Rules require the originator to make changes or corrections within six (6) banking days of receiving the information from the *Bank* or before another entry is sent.
- The Receiving Bank warrants that the Information they provide to you is correct.
- The *Bank* may pass along any fines received based upon your non-compliance.
- The Originator has the option of responding to NOCs for Single Entry (non-recurring) payments. This applies to the following SEC Codes only: ARC, BOC, POP, POS, RCK and XCK entries, as well as, TEL and WEB entries bearing a single entry indicator ("S" or "blank" for TEL and "S" for WEB).

### Notification of Change (NOC) Codes (most common)

NOC Code	Reason	Description
C01	Account Number	Account number is incorrect or is formatted incorrectly.
C02	Transit/Routing Number	Due to a merger or consolidation, a once valid routing number must be changed.
C03	Transit/Routing Number and Account Number	Due to a merger or consolidation, a once valid transit/routing number must be changed and the account number structure is no longer valid.
C04	Account Name	Customer has changed name.
C05	Transaction Code	Transaction code is incorrect and this is causing the ACH entry to be routed to the wrong application (demand or savings).
C06	Account Number and Transaction Code	Account number is incorrect or is formatted incorrectly and the transaction code is incorrect causing the ACH entry to be routed to the wrong application (demand or savings).
C07	Transit/Routing Number, Account Number and Transaction Code	Due to a merger or consolidation, a once valid transit/routing number must be changed, the account number structure is no longer valid and the transaction code is incorrect causing the ACH entry to be routed to the wrong application (demand or savings).
C09	Individual Identification Number	The individual id number was incorrect.
C13	Addenda Format	Information in the Entry Detail Record was correct and the entry was processed and posted by RDFI. However, information found in the addenda record was unclear or was formatted incorrectly.

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### Reversals

- If a reversing entry must be made, please consult the ACH Manager User Guide or contact Customer Service for instructions.
- Reversals may only be made for the following three conditions:
  1. wrong dollar amount
  2. wrong account number
  3. duplicate transaction
- When initiating a reversal, the reversing entry must be for the full amount, must be sent within five (5) banking days of original entry and must be sent within 24 hours of discovering the error.
- The Receiving Bank is under no obligation to post the reversing debit if it overdraws the payee's account or if the payee's account is closed.
- A payee must be notified if a reversing entry debits his or her account. However, a payee does not need to authorize the reversing debit.
- The word "REVERSAL" must be placed in the Company Batch Header Field and if the file is reversing an erroneous file, then a correcting file must be initiated with the reversing file

### OFAC (Office of Foreign Asset Control)

- You are required to check payees against OFAC compliance checklists.
- OFAC lists countries, groups and individuals with which U.S. Companies are not permitted to send or receive funds.
- The *Bank* must protect itself by informing every client that it is against the law to send debit or credit entries to OFAC-blocked entities.
- You may check the OFAC SDN list at: <http://sdnsearch.ofac.treas.gov>

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#### **What are the Fraud Risks for ACH?**

ACH Origination fraud is a challenge for Financial Institutions and ACH Originators like your company. In one origination system hacking scheme, perpetrators hack into the originator's (your company) computer system using compromised User IDs and passwords and originate ACH credits to "mule" accounts created for the express purpose of committing fraud. Those accounts are then emptied and abandoned. The true originator's account (your account) is debited for the invalid origination file. The credits are usually irretrievable by the time the fraud is discovered. The originator's credentials may have been compromised by an insider within the organization or stolen through key loggers or Trojan Horse programs on the compromised computer.

Due to the risk of this type of fraud, it is essential that all computer equipment used by your company to operate North Star Bank's Cash Management ACH Origination program is regularly updated and patched for security vulnerabilities (including the use of and updating of firewall, virus protection, anti-malware protection, anti-spam protection.) You may also want to consider having one computer in your office which is not used to browse the internet or read e-mail to be your sole source of access to the Cash Management system. Limiting access to the computer which is used to house and transmit ACH data may help avoid the accidental downloading of harmful programs/viruses that could potentially compromise your transactions.

The appropriate steps should be taken within your company to ensure that all User ID's, Passwords, Authentication Methods and any other applicable security procedures issued to your employees are protected and kept confidential. All staff should be aware of the need for proper user security, password controls and separation of duties.

As ACH Origination is a higher risk commercial banking function, we suggest that your company perform your own internal risk assessment and controls evaluation periodically to be sure you are considering all available security options.

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### **What types of controls are in place to help combat ACH Origination fraud?**

The Bank's ACH Origination system requires the use of a token which creates a random code to be used in conjunction with your User ID and PIN. While this will hamper a hacker from gaining access outside of your company, the risk still exists for internal fraud by one of your employees or from a hacker who had gained access to your computer system through sophisticated key loggers or Trojan Horse programs.

North Star Bank (Bank) strongly encourages companies to have separation of duties for ACH processing, in which one employee generates the ACH batch and the system requires a secondary employee to log in and approve the ACH batch. Dual-approval procedures such as this go a long way in preventing ACH origination fraud. If you don't currently have the Dual-approval security feature in place, you can request to enable it by contacting Bank's Cash Management Department to discuss the options available.

Cash Management ACH transaction rights are limited to personnel with appropriate business need for functionality. Company ensures that all individuals with access to the Cash Management program received training necessary to understand their responsibilities and utilize the program in accordance with the applicable terms, agreements and ACH rules.

It is also very important for your company to make it a practice of monitoring your accounts online daily. Reviewing both the balances and the account transaction daily within the Cash Management system will ensure that you are aware of all transactions, even when they have not yet posted to your account. The sooner account or ACH fraud can be detected, the more successful the bank will be in assisting to recover your company's potentially lost funds.

North Star Bank has security alerts available for you to enroll in to send notifications when your password has been changed, or when an outgoing ACH transaction has been generated.

Please keep in mind that we will **never** email you requesting your Cash Management password or token credential. We may on occasion call to verify other information regarding your on line activity should we see something of concern in your login patterns.

### **What happens if a Security Breach occurs?**

Immediately contact the bank if you suspect an ACH data breach. As an ACH Originator, you are required to immediately report the breach to North Star Bank who must report it to NACHA.

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#### **ACH Rule Changes and Rules of Awareness**

The National Automated Clearing House Association (NACHA) is the rule making body governing the ACH network and therefore all participants of the ACH network must comply with the NACHA Operating Rules. Each company sending ACH entries through North Star Bank using its Cash Management ACH Origination program must comply with the NACHA Operating Rules as stated within the ACH agreement between North Star Bank and the Corporate Customer.

North Star Bank will annually communicate applicable Operating Rules changes to ensure that our companies are educated on those Rules and make any necessary changes to its daily process as a result of these changes. Annually, you may purchase copy of the updated NACHA Operating Rules & Guidelines by visiting [www.nacha.org](http://www.nacha.org) or you may obtain free limited access to the basic NACHA Operating Rules in read-only format by visiting [www.achrulesonline.org](http://www.achrulesonline.org).

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#### **Right to Audit / NACHA Enforcement Authority**

Upon written request, North Star Bank shall have the right to examine your ACH Operations to ensure that ACH data is being processed correctly and that processing is adequate to meet the terms of our agreement and all NACHA Operating Rules. North Star Bank may voluntarily provide to NACHA, information such as return data that may be indicative of a potential Rules violation by any of our customers.

If you have any questions relating to ACH Origination Rules, please contact North Star Bank's Cash Management Department at 1-651-489-8811.