



ACCOUNT VALIDATION: A TOOL FOR BUSINESSES TO IMPROVE ACH TRANSACTIONS



With Contributions from the NACHA Board Advisory Group

ABOUT “ACCOUNT VALIDATION: A TOOL FOR BUSINESSES TO IMPROVE ACH TRANSACTIONS”

NACHA — The Electronic Payments Association developed this paper in conjunction with the Payments Innovation Alliance and the NACHA Board Advisory Group. The goal of this paper is to highlight what methods of account validation are available today and provide information on possible future options that the industry may want to pursue.

ABOUT NACHA – THE ELECTRONIC PAYMENTS ASSOCIATION

Since 1974, NACHA – The Electronic Payments Association has served as trustee of the ACH Network, managing the development, administration and rules for the payment network that universally connects all 12,000 financial institutions in the U.S. The Network, which moves money and information directly from one bank account to another, supports more than 90 percent of the total value of all retail electronic payments in the U.S. Through its collaborative, self-governing model, education, and inclusive engagement of ACH Network participants, NACHA facilitates the expansion and diversification of electronic payments, supporting Direct Deposit and Direct Payment via ACH transactions, including ACH credit and debit payments, recurring and one-time payments; government, consumer and business transactions; international payments, and payments plus payment-related information. Through NACHA's expertise and leadership, the ACH Network is now one of the largest, safest, and most reliable systems in the world, creating value and enabling innovation for all participants. Visit www.nacha.org for more information.

ABOUT THE NACHA BOARD ADVISORY GROUP

NACHA has continually engaged business end users, processors, solution providers and others through membership programs, industry outreach, and various groups and channels within NACHA rulemaking on the development of the ACH Network and the NACHA Operating Rules. As a natural progression of this engagement, NACHA formed the Board Advisory Group as a formal venue for senior executives from a balanced cross-section of non-financial institution providers and end users of the ACH Network to communicate directly with the NACHA Board of Directors on ACH payment priorities, needs and capabilities from the perspective of end-user clients and the technology firms that enable them. The Board Advisory Group is yet another way in which NACHA reaches out and listens to various stakeholders across the payments ecosystem, underscoring its commitment to the direct and inclusive engagement of the payments end-user and solution provider communities.

ABOUT THE PAYMENTS INNOVATION ALLIANCE

The Payments Innovation Alliance brings together diverse, global stakeholders to support payments innovation, collaboration, and results through discussion, debate, education, networking, and special projects that support the ACH Network and the payments industry worldwide. The Alliance brings together content and focus across all payment areas, including emerging payment technologies, electronic billing and presentment, mobile, payment security/risk, check conversion and global payments. Membership includes organizations of all sizes and spans the payments industry spectrum.

For more information about account validation, companies should contact their financial institution or technology provider and visit NACHA's website at www.nacha.org/content/corporate-relations.

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Ali Ashraf

Manager, Business Intelligence & Analytics
Target Corporation

David Barnhardt

Vice President, Product Management
Early Warning Services LLP

Ann-Marie Bartels, AAP

Chief Executive Officer
EPCOR

Pam Cerny, AAP, CTP

Director of Training
SWACHA

Frank D'Amadeo

Director, Treasury Operations
Con Edison

Noelle Donselaar, AAP

Governance, Policy & Risk
Capital One

Paula Epstein, AAP, CTP

VP, ACH Product Manager
TD Bank, N.A.

Daphne Gilliam, AAP, CCM

VP, ACH Product Manager
PNC Bank

Rob Harris

VP, Product Management
FIS

Walt Henderson, AAP

Director, EFT Strategy Division
U.S. Dept. of Treasury, BFS

Hali Jewell, AAP

Product Management
Fiserv

Fred Laing, AAP, CCM, NCP

President
Upper Midwest ACH Association

Bill Phillips

Group President, Ent. Pay. Solutions
ProfitStars – a Jack Henry Company

Alan Reed

Lead Rem. Op. Sys. Support
AT&T

Muneeb Iqbal Shah

Consulting Manager, Treasury & Payments
Wipro LTD

Todd Wachob

Sr. Mgr., Credit Risk Management
PAYCHEX, Inc.

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Note: The views presented in this paper do not necessarily reflect the individual views of each member of the task force listed above, the entities or organizations that employ the members of the task force, the NACHA Board Advisory Group, or the Board Advisory Group member organizations.

INTRODUCTION TO ACCOUNT VALIDATION

Account validation is an important tool for businesses who originate ACH credits and debits. Using an incorrect routing and transit number and/or account number for the recipient of an ACH transaction can cost a business both time and money. It can damage a company's relationship with employees, customers and vendors; result in fees from a company's financial institution; delay the start of an employee's direct deposit of payroll; cause payments to suppliers to fail; and delay in the collection of funds from customers. Using account validation enables businesses to reduce returned transactions, in cases where an account number was incorrectly entered, and fraudulent payments, where the wrong account number was purposefully entered. It also helps to provide a positive customer experience while reducing the number of customer service calls and lost customers.

NACHA has been focused on this topic for several years, with a goal of increasing the quality and security of ACH transactions through improved account validation practices. In 2012, NACHA identified account validation as critical to the long-term support of payment innovation, user enablement, and ACH origination. Through surveys, forums and one-on-one meetings with businesses, financial institutions and solution providers, the industry has made it clear that there is a need and a desire for improved account validation services.

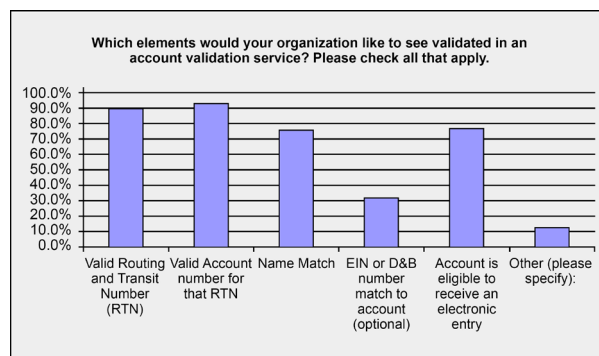
In a 2012 industry survey, when asked about capabilities needed long term for the ACH Network, account validation was the highest rated need overall, in addition to it being rated highest by companies. In the 2015 industry survey, when asked about several topics (tokenization, payments information and messaging, ISO 20022 adoption, directory services and account validation) and their importance, account validation was the highest priority among all groups (e.g., financial institutions, solution providers, and companies). It seems clear that all segments of the industry continue to be interested in account validation.

ACCOUNT VALIDATION SURVEY

In 2013, NACHA conducted a survey on account validation with financial institutions, solution providers and businesses, in order to better understand the needs and preferences for account validation in the industry. In general, respondents felt there was a need for more education on how the different options for account validation work, were interested in more ubiquitous solutions, and felt that speed and level of information varied depending on the use case.

Survey respondents agreed almost unanimously with the following definition of account validation:

A service wherein a business or financial institution can validate the accuracy of the account information received from a consumer or business, and the ability of that account to receive electronic payments.



The results of the survey were not quite as clear cut on the topic of what needs to be validated. Around 90% of respondents agreed it was necessary to validate that the routing and transit number (RTN) was a valid RTN, and that the account number provided was valid for that specific RTN. Close to 80% also wanted to do some sort of name match, and verify that the account was "ACH-able" meaning that it could receive electronic debits and credits. However, the 80% that would like a name match also acknowledged that providing that match would not

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be an easy task for financial institutions, given the endless variations in individual and company names. Some corporate respondents also wished to receive additional information for some use cases such as validating that the Employer Identification Number (EIN) or Dun & Bradstreet (D&B) number matched, funds availability, date of last transaction on account, number of returns on account, account type, etc.

The results around the necessary timing also varied, although in general, faster was perceived as better. The majority of respondents desired a response in either real time (defined in the survey as within 30 seconds), same day, or next day. However this question was not broken down by use case which impacts how quickly a response is truly needed.

Although specific needs for account validation vary, the industry does seem to agree that ACH transactions, both credits and debits, for both business and consumer payments, would be better served if bank account information were validated consistently by companies.

USE CASES FOR ACCOUNT VALIDATION

RECURRING PAYMENTS

Recurring debits and credits are among the most widely used transactions in the ACH Network. The frequency of validation for the use cases below varies, with some companies only validating the payment information at enrollment and others validating before each payment is sent. It is up to each company to decide how frequently account validation should be performed for a recurring payment. It is also important for a business to ensure correct procedures are in place to make necessary updates to account information when your customer or your financial institution notifies you of changes.

Remember that when sending ACH transactions, it is desirable to validate not only account information, but also account ownership, if possible. It should be noted that there are several different methods of account validation that a company can choose to employ, each with their own pros and cons.

Below are some common use cases for recurring ACH debit and credit transactions.

CONSUMER DIRECT PAYMENT Consumer authorizes company to initiate recurring debits to account such as monthly bill payments	CONSUMER LOAN PAYMENT Consumer authorizes financial institution to initiate recurring debits to account to make loan payments	CONSUMER PHYSICAL POINT OF SALE Consumer enrolls with merchant to authorize debits to account when making purchases at the physical point of sale
CONSUMER MOBILE WALLET Consumer enrolls with issuer of wallet to authorize debits to account when wallet is used for a purchase or bill/P2P payment	CONSUMER ONLINE TRANSACTIONS Consumer authorizes the merchant to initiate debits to account when a purchase is made online	H2R* PAYROLL FUNDING Company authorizes payroll service provider to initiate debits to account to fund payroll credits to employees
	H2R* DIRECT DEPOSIT Consumer provides the necessary information for company to initiate credits to account, such as payroll	

*H2R = Hire to Retire

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In recurring transaction use cases, account validation occurs during an enrollment process, before the initiation of the first transaction, or on a scheduled basis prior to the payment being sent. Account validation therefore is not required to be real time. In general, however, same day or next day is preferred by companies in order to ensure a good customer experience. In each of the use cases listed above, account validation is used to help prevent fraud and reduce errors.

ONE TIME PAYMENTS

For each of the one-time payment use cases listed below, a company would want to validate the payment information prior to initiating the debit or credit. When sending ACH transactions, it is desirable to validate not only account information, but also account ownership, if possible. It should be noted that there are several different methods of account validation that a company can choose to employ, each with its own pros and cons.

Below are some common use cases for one-time ACH debit and credit transactions.

CONSUMER ACCOUNT FUNDING Consumer opens new account and moves money from another financial institution to fund the new account	CONSUMER ONLINE PAYMENT Consumer authorizes company to initiate a debit to account when making a purchase or paying a bill	CONSUMER EXPEDITED PAYMENT Consumer authorizes company to initiate a same day debit to account when making a purchase or paying a bill point of sale
CONSUMER REBATES AND REFUNDS Consumer provides the necessary information for company to initiate a credit to account	P2P* DISBURSEMENTS Consumer or company provides necessary information for company to initiate an owed credit to account	CONSUMER LOAN PAYMENT Consumer sends credit from account at one financial institution to pay a loan held at another financial institution

*P2P = Procure to Pay

There is no enrollment process for a one-time payment, so quicker account validation is often desired to mitigate risk for ACH transactions. Faster is preferred, with a minimum response time of same day or sooner, in order to keep the process moving, to provide a good customer experience, and to ensure the information is verified prior to shipping goods or continuing to provide services. In each of the use cases listed above, account validation is used to help prevent fraud (including “friendly fraud”, when a customer provides the business with wrong account information with the intent to gain time to make the payment) and reduce errors. Additionally, in the case of account funding, it enables faster access to funds.

The following infographic illustrates currently used methods of account validation.

CURRENTLY USED METHODS FOR ACCOUNT VALIDATION



MANUAL METHODS

How it WORKS

A company uses consumer's check to verify account information and uses identification to confirm consumer identity, and/or company calls the consumer's financial institution.



To IMPLEMENT



Company must create procedures and train employees on how to verify information on check/identification and/or call financial institutions

ACH VALIDATION TEST

How it WORKS



The ACH Network connects to all financial institutions across the U.S. Companies can send a prenote through the ACH Network to their customer's bank and verify the accuracy of bank account information.

To IMPLEMENT



Work with financial institution or vendor to be able to send prenotes for new or changed transactions

MICRO DEPOSITS THROUGH ACH

How it WORKS

A company sends one or two very small credit ACH transactions (and sometimes a debit to remove the money) to their customer. The customer informs the company what amount(s) were deposited to and debited from their account. This verifies the account number and ensures the customer has ability to view the account.



To IMPLEMENT



Set up internal procedures for initiating small credit and debit entries and a simple method for customers to confirm amounts

VALIDATION SERVICES

How it WORKS



Some financial institutions and third parties have access to a large number of accounts (both their own and others) and may offer a product that leverages this information. A company can access these services for scoring as to the likelihood of correct account information and/or the account holder's identity. These responses can be real-time, same-day or next-day and can do many things besides validate the account number and ownership, including provision of information on the account itself (age, returns, etc.).

To IMPLEMENT



Contact your financial institution or third party to learn more about accessing these systems and make any necessary changes to in-house systems

For more information about account validation, companies should contact their financial institution or technology provider and visit NACHA's website at www.nacha.org/content/corporate-relations.

PROS AND CONS OF METHODS OF ACCOUNT VALIDATION

Each of these methods has pros and cons and each works best for different use cases:

MANUAL METHODS

- Manual methods work to verify information and identity, but are very time consuming and don't scale well. Also, financial institutions may not be willing to provide information to a caller, and it may be difficult to get consumers to provide a check – some financial institutions no longer provide them for all accounts.
- Best for use cases with small number of new accounts to verify at one time.

VALIDATION ENTRY THROUGH THE ACH

- Verifies RTN and account number are for an open account that can receive an ACH entry, but does not check the name. It is a “no news is good news” model with no definite yes/no response back. Waiting period for response is 3 days.
- Best for use cases where the business can wait several days before initiating an entry.

MICRO DEPOSITS

- Verifies RTN and account number are for an open account that can receive an ACH entry, and that the Receiver has access to the account. It can take several days as the business must wait for a consumer's response, and many consumers view the process as too burdensome and don't complete it.
- Best for use cases where the business can wait several days before initiating the first transaction and a consumer is willing to make an effort to enroll.

VALIDATION SERVICES

- Fast and effective, but a limited number of third parties and financial institutions provide the service, and scoring technology is still new and not widely available to corporates. Companies must provide information on customers, and this may require compliance with additional regulation and carry potential risk. These services can be viewed as cost prohibitive.
- Best for use cases where speed of response and/or additional information about the account and account holder is critical.

In addition to the methods already illustrated, there are “sign-in” or “instant” verification methods, which require a consumer to provide his/her online banking credentials so an account validation solution provider can login as the consumer to check the account information and validate the consumer’s identity. These solutions are effective and easy for the consumer to use, but increase the risk of financial information falling into the wrong hands. Companies who utilize third parties for these account validation solutions need to be sure to perform the appropriate due diligence and weigh any accompanying risks to themselves or their customers. It is not considered an industry best practice for consumers to give out their online banking credentials, and, in fact, some financial institutions spell out in their agreements the consumers’ liability if they do so. In addition, use of these types of applications can increase abandonment rates, as many consumers are hesitant to provide this information. There can also be issues with these systems not operating efficiently, to the point that some financial institutions have felt it necessary to cut off access to account information temporarily.

OPPORTUNITIES ON THE HORIZON

In addition to the account validation methods available today, the industry is pursuing several opportunities to improve current methods and/or create new possible solutions. The advent of Same Day ACH will significantly shorten the length of time needed to achieve validation through micro deposits or prenotes. In addition, NACHA is looking at the possibility of creating a new type of prenote entry with a goal of releasing a Request for Information to the industry for comment by late 2016. Use cases will be identified for a same day validation that includes a positive or negative response.

New solutions are also being pursued, such as a standardized Application Programming Interface (API) for account validation. An API is a set of protocols and tools used to develop software and applications, and is a method for applications to share data. Financial institutions have the ability to develop APIs which allow service providers or companies to code to that API to access bank data for a customer. If there were a standard API developed, service providers and companies would only have to code to one standard API to have it work with all financial institutions. An API library could be formed with various requests such as balance, history, account holder information, etc. In the future, account validation could even be used for things other than payments such fighting fraud or performing credit checks.

Several groups are investigating API technology and standards for account validation messaging, including the World Wide Web Consortium’s (W3C’s) consideration of the OAuth authentication protocol. The use of standardized API’s would provide safe, secure ubiquitous account validation. Financial institutions would maintain control of the financial data and ensure protection of consumer credentials that use third party services. NACHA is a part of this ongoing effort and will continue to communicate with the industry as these new solutions evolve.

CONCLUSION

Companies experiencing issues with fraud or exceptions should consider using some method of account validation before initiating ACH transactions. There is not necessarily one ideal solution for every type of transaction, so it may be necessary to use different types of account validation for different use cases and businesses must decide what method or methods best meet their needs.

To help determine if account validation needs to be used for ACH credits and debits originated, a company may wish to create a business case. The business case should include both the cost of implementing an account validation system, and the potential losses avoided through its utilization, such as employee time, damage to company's relationship with customers, vendors and employees, financial institution fees, delays in receipt of funds from customers, and lost customers.

Several methods of account validation currently exist and can be utilized. Additionally the industry is pursuing several efforts to improve current options or create new solutions. However, this will be a large task and require a substantial effort from all stakeholders: financial institutions, processors/vendors, and businesses.

For more information about account validation, companies should contact their financial institution or technology provider and visit NACHA's website at <https://www.nacha.org/content/corporate-relations>.