

# Examining ACH risk ...to be better prepared

For effective risk mitigation, knowing what is at risk is half the battle. Gaining an understanding of what external regulators look for during a routine bank examination regarding ACH risk can help position financial institutions to be better prepared to mitigate risk.

## Types of ACH risk

For originating depository financial institutions (ODFIs), the first step toward monitoring ACH risk is knowing what risks apply to every ACH operation. Careful monitoring of risk can put your organization in a proactive risk mitigation position for both origination and return transactions. Types of ACH risk include:

- Credit risk—the risk that an ACH originator does not have the necessary funds on the settlement date
- Fraud risk—the risk that an ACH payment will be generated or altered in a deliberate attempt to misdirect or misappropriate funds
- Operational risk—stems from data entry errors, as well as hardware or software failures, that may delay or alter an ACH transaction

Bank examiners and auditors often assess ACH risk and set examination schedules based on the size, scope and nature of an ODFI's ACH business. They may compare an ODFI's ACH transaction volume to that of peer institutions and investigate the types of ACH transactions processed (e.g. WEB, TEL, PPD, BOC, ARC, POP).

ODFIs should monitor ACH payments in accordance with the type of transactions, the complexity of processing relationships and the financial exposure. For example, a large volume of one-time ACH payments, such as TEL transactions originated by a third party on the ODFI's behalf, are considered riskier than scheduled recurring payments. Examiners try to ensure that a financial institution's risk management tools adequately address these variations and complexities in ACH transactions.

### Helpful resources

The OCC's *Bulletin 2006-39 Automated Clearing House Activities: Risk Management Guidance*, available at [www.occ.treas.gov/ftp/bulletin/2006-39.pdf](http://www.occ.treas.gov/ftp/bulletin/2006-39.pdf), is a useful guide to establishing an effective ACH risk management program. The guidance advises that effective risk management programs include written policies and

The FedACH Risk Origination Monitoring Service allows Subscribers to preset debit and credit caps on ACH origination, hold for decisioning batches that exceed these caps and e-mail designated contacts. This service allows the ODFI to evaluate its credit, fraud or operational risk exposure for all these held batches, regardless of the complexity of the processing relationships. Subscribers can choose to monitor all originators, thereby preventing ACH origination from a company ID not defined, or to monitor specific originators using monitoring criteria customized by company identification number. The ODFI can also choose to monitor across an entire routing transit number (RTN) in order to keep track of its Federal Reserve account exposure. With this powerful tool, Subscribers can monitor credit and debit totals over a single day or across multiple processing days to better manage overall ACH risk exposure.

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procedures, strong internal controls and risk-based audit programs. It also explains how to establish underwriting standards and approval policies for ACH originators.

Another helpful resource is the FFIEC's *Information Technology Examination Handbook*, available at [www.ffiec.gov/ffiecinfobase/html\\_pages/retail\\_book\\_frame.htm](http://www.ffiec.gov/ffiecinfobase/html_pages/retail_book_frame.htm). Specifically, the "Retail Payment Systems" section contains detailed information on the various types of risk and risk management controls, and is an excellent guide for both bankers and examiners.

### Federal Reserve risk tools

The Federal Reserve Banks are helping ODFIs mitigate ACH risk by offering a suite of FedACH Risk Management Services that provides ODFIs with tools to monitor ACH risk from simple transactions to the more complex ACH transaction types and processing relationships. These tools enable ODFIs to monitor ACH risk from various points of view: its own perspective toward risk and the examiner's perspective toward effective monitoring programs.

The FedACH Risk Returns Reporting Service via FedACH Information Services enables ODFIs to produce reports of returns by originator for either a single day or up to a 10-day processing date range within the previous 60 business days. This flexible service provides Subscribers with the ability to establish thresholds at which an originator's return volume will appear on a report. For unauthorized returns (return reason codes R05, R07, R10, R29, R51), as well as for administrative returns (return reason codes R03, R04), Subscribers are able to set a reporting threshold as low as one return.

To find out more about FedACH Risk Management Services, visit [www.frbservices.org/Retail/fedachRisk.html](http://www.frbservices.org/Retail/fedachRisk.html) or contact your FedACH Sales Specialist via *My FedDirectory* on [www.frbservices.org](http://www.frbservices.org).