Universal Application of the Rules
Request For Comment

Executive Summary and Rules Description
October 1, 2010

COMMENTS REQUESTED BY FRIDAY, OCTOBER 29, 2010.
NACHA requests comments on a proposal to amend the NACHA Operating Rules entitled “Universal Application of the Rules.” Comments are due by Friday, October 29, 2010.

NACHA STAFF CONTACTS
Return comments to:   Maribel Bondoc, Manager, Network Rules
Fax (703) 787-0996
E-mail:  mbondoc@nacha.org

Questions:       Michael Herd, Managing Director, ACH Network Rules
Phone (703) 561-3924
E-mail:  mherd@nacha.org

Part I: Proposal Brief

This rules proposal (“Rule”) recommends changes to the NACHA Operating Rules (“Rules”) so that the Rules would apply uniformly to all transactions that use the NACHA formats or SEC Codes, or rely on the Rules, regardless of how such transactions are cleared and settled between financial institutions.

Part II: Background

Historically, ACH transactions were transmitted between participating DFIs through an ACH Operator. Accordingly, the Rules are based on the assumption that an entry will be transmitted to an ACH Operator for routing to an RDFI or ODFI. Since the Rules were originally written, there have been many changes in the ways the ACH transactions are processed, and the Rules acknowledge many other types of processing arrangements or entities.

Today, while most ACH transactions are still processed by an ACH Operator, the manner in which Participating DFIs exchange transactions has evolved so that some transactions are not. In some cases, ACH transactions are exchanged directly between two participating DFIs; in other cases, ACH transactions are exchanged among participating DFIs within a closed network. ACH

---

1 Examples in the Rules are: 1) Sending Point; 2) Receiving Point; 3) Third Party Service Provider; 4) Third Party Sender; and 5) Direct Access.
transactions might also remain within a single financial institution (on-us) and these also are not processed through an ACH Operator.

The Rules, however, do not contemplate the processing of ACH transactions without the involvement of an ACH Operator. The Rule described within this Request for Comment is intended to ensure that the Rules are applied consistently to all ACH transactions, regardless of how they are processed between financial institutions. These changes would uphold the applicability of the Rules to all transactions, and provide certainty that the Rules apply in the event of any legal questions or disputes.

By promoting consistency, the changes also would help prevent customer confusion and dissatisfaction that may arise from disparate treatment of transactions that customers expect to be subject to a single framework established under the Rules. Finally, these changes would advance the role and effectiveness of private-sector rulemaking, in which financial institutions agree to self-regulate, adopting standards and practices that are in the best interests of the ACH Network as a whole.

These goals would be accomplished both by ensuring that all such transactions, regardless of the processing channel, are subject to the Rules, and by ensuring that NACHA has the authority to enforce the Rules with regard to all such transactions.

**Part III: Rules Framework and Implementation**

*Elements of the Proposal*

- The Rule would clarify that the Rules apply to all entries, not just entries that are processed through ACH Operators;
- The definition of “Entry” would be modified to include transactions that use the NACHA formats, SEC Codes, or that incorporate, refer to or rely on the Rules;
- New definitions for entries that are not processed through ACH Operators would be added (“On-Us Entry” and “Non-Operator Entry”);
- Provisions would be added describing the application of the Rules to Non-Operator and On-Us Entries;
- The Rule would clarify that an ACH Operator’s settlement obligations apply only to entries processed by that ACH Operator.

*Application of the Rules*

Currently, the Rules apply to “all Entries Transmitted through one or more ACH Operators.” This rule reflects the historical ACH transaction flow, in which all transactions that relied on NACHA formats were processed through ACH Operators. Over time, the arrangements through which such transactions are transmitted between participating DFIs have evolved. Because these transactions do not flow through an ACH Operator, however, it may be argued that they are not subject to the Rules as presently written.

---

2 2011 NACHA Operating Rules, Section 1.1, Application of the Rules.
Transactions that are not transmitted through ACH Operators, but are commonly understood to be “ACH” transactions, use the NACHA formats, utilize SEC Codes, are originated under agreements that reference or incorporate the Rules, and are otherwise indistinguishable to originators and receivers from those transactions that are processed through ACH Operators. If such transactions are treated differently, customers may become confused and dissatisfied with ACH payments. For example, a company submitting an ACH payroll file to its ODFI may reasonably expect consistent treatment of the transfers to their employees regardless of where the employee holds an account and regardless of the flow of the transaction. As a further example, a participating DFI may look to the Rules for certainty to determine how to process a transaction and understand its liability for that transaction, only to have it argued subsequently in a dispute that the Rules do not apply.

Therefore, to ensure that all transactions that rely on the NACHA formats and SEC codes are covered by the Rules, this Rule proposes to delete the out-dated limitation that applies the Rules only to entries that are transmitted through ACH Operators, and instead apply the Rules to all entries.

**Definition of Entry**

This Rule proposes to apply the Rules to all entries, rather than just entries that are transmitted through ACH Operators. Without the language limiting the application of the Rules to those entries that flow through ACH Operators, it is important to clearly define the scope of the transactions to which the Rules apply.

The Rule proposes to modify the definition of “Entry” to reflect the scope of transactions that should be subject to the Rules - specifically, transactions that (1) are formatted in accordance with certain NACHA formatting requirements; (2) utilize or rely on a definition of an SEC Code; or (3) are originated or transmitted under an agreement that incorporates or references any provision, section or requirement of the Rules.

**Definitions of “Non-Operator Entry” and “On-Us Entry”**

To accurately describe the application of the Rules to entries that are not processed through an ACH Operator, the Rule proposes two new definitions: “Non-Operator Entry” and “On-Us Entry.” A “Non-Operator Entry” would be the term used to describe any entry that is not processed by an ACH Operator. An “On-Us Entry” would be a specific kind of Non-Operator Entry for which the account of the originator and the account of the receiver are held by the same participating DFI.

**Application of the Rules to Non-Operator Entries and On-Us Entries**

As described above, the Rules are currently written to reflect an ACH processing flow in which all entries are processed through an ACH Operator. There are numerous provisions throughout the Rules that specifically reference ACH Operators, and so therefore do not address the possibility that an ACH entry could be processed without an ACH Operator. For example, the
timeframe for an RDFI to return an entry is stated in reference to an ACH Operator: “An RDFI must Transmit a Return Entry to its ACH Operator by the ACH Operator’s deposit deadline…”

To achieve the stated goal of consistently applying the Rules to all entries, this Rule proposes to clarify the application of the Rules to those entries that are not processed through an ACH Operator. Specifically, the following new general provisions would interpret the application of the Rules to non-operator entries:

- Participating DFIs involved in a non-operator entry are not relieved of their obligations under the Rules to the originator or the receiver;
- Participating DFIs involved in a non-operator entry may satisfy any requirement of the Rules that references a transmission or delivery to an ACH Operator by direct communications between the ODFI and RDFI (or through the DFI’s internal process for an on-us entry), as long as any timing or other requirements are met;
- A participating DFI involved in an on-us entry is not relieved of its obligations as the ODFI and RDFI;
- A participating DFI involved in an on-us entry would represent to NACHA that all warranties applicable to the entry are true and accurate, even though the same DFI is otherwise both the maker and the beneficiary of the warranty;
- NACHA may enforce a participating DFI’s compliance with the Rules for a non-operator entry as set forth in Appendix Ten of the Rules without receipt of complaint from another participating DFI.

These new provisions would enable the Rules to be applied, interpreted and enforced consistently without regard to the processing channel.

Settlement

Because the Rules are generally based on the assumption that an entry will be transmitted through an ACH Operator, the settlement obligations of ACH Operators currently are written to apply to all entries. In light of the modifications to the definition of “Entry” and the clarification that the Rules apply to entries that are not processed by an ACH Operator, the Rule would clarify that the entries that are subject to an ACH Operator’s settlement procedures are the Entries that are processed by that ACH Operator, and that the entries an ACH Operator is responsible for settling are the entries that are transmitted through that ACH Operator.

Part IV: Impact of the Proposal

Benefits of the Proposal

This Rule addresses the consequences that would arise if Participating DFIs differentiated their treatment of ACH transactions on the basis of the processing channel used for the transaction, and the consequences of relying on the Rules for certainty only to have it argued subsequently in a dispute that the Rules do not apply. These consequences could include an uncertain legal status in the event of a dispute or legal action, customer confusion and dissatisfaction, lack of Rules

---

3 2011 NACHA Operating Rules, Section 3.8, RDFI’s Right to Transmit Return Entries.
enforcement, and an adverse impact on the credibility and effectiveness of private-sector rulemaking. The changes proposed in this Rule are intended to ensure that all such transactions are treated consistently, are consistently upheld in the event of legal questions, and preserve the quality of such transactions.

**Costs to Comply with the Proposal**

As the Rule involves definitions and coverage, there are no direct costs to comply with the Rule. A participating DFI may be impacted, however, if it currently processes what would be defined as non-operator entries in any manner that is not consistent with the Rules.

**Part V: Effective Date**

The Rule is proposed to become effective on March 18, 2011.

**Part VI: Other Issues**

The topics listed below are related to the Rule proposal, but are not being addressed with specific Rules language. NACHA invites additional comment on these issues that can be considered in deciding whether to address these topics in the Rules.

**Non-ACH Operator Processing Entities**

This Rule concerns the consistent coverage of the Rules to all entries, regardless of how the entries are processed between financial institutions; i.e., the entries may be processed by some entity other than an ACH Operator acting as an intermediary among financial institutions. Currently, no other type of such processing entity is defined in the Rules. NACHA invites comment on how the Rules should ultimately acknowledge and define such entities, and what types of obligations should be established, such as ACH file editing, specific settlement responsibilities, and specific reporting to NACHA for purposes of ACH Network risk management.

**Transaction Reporting**

Currently, the ACH Operators provide to NACHA aggregate data on the volume of ACH entries and returns by SEC Code. This data is critical to the industry’s understanding of the uses, the quality, and the entirety of the scope of the ACH Network. NACHA invites comments on how the Rules should address similar types of transaction reporting by participating DFIs that are involved in non-operator entries to ensure that the industry continues to have a complete view of the ACH Network.

---

4 Under the Rules, the ACH Operators perform a number of ACH file edits that serve the purposes of transaction quality and Rules compliance. See 2011 NACHA Operating Rules, Appendix Two.

5 Under the Rules, the ACH Operators have specific settlement responsibilities. See 2011 NACHA Operating Rules, Article Seven.
Part VII: Technical Summary

The following changes to the technical language within the Rules are included in this proposal:

- Article One, Subsection 1.1.1 (Application of Rules) – Deletes reference to ACH Operators so that the Rules apply to all entries regardless of the clearing channel.
- Article One, Section 1.1.3 (Application of Rules for Non-Operator Entries) – Adds a new subsection to clarify the manner in which the Rules will be interpreted to apply to entries that are not cleared through an ACH Operator.
- Article One, Subsection 1.1.3.1 (Application of ACH Operator Provisions for Non-Operator Entries) – Adds provision clarifying that internal processes of the Participating DFI may satisfy procedural requirements of the Rules involving ACH Operators for on-us entries, and processes established between an ODFI and RDFI may satisfy the procedural requirements of the Rules involving ACH Operators for other non-operator entries.
- Article One, Subsection 1.1.3.2 (Obligation of Participating DFI as ODFI and RDFI) – Adds an express statement that the Participating DFI of an on-us entry is not relieved of its obligations as an ODFI and RDFI under the Rules, and allows NACHA to enforce a Participating DFI’s compliance with the Rules.
- Article One, Subsection 1.1.3.3 (Application of Warranties for On-Us Entries) – Adds a provision that the Participating DFI of an on-us entry has an obligation to ensure that each warranty made by an ODFI or RDFI with respect to the entry is true and accurate.
- Article Seven, Subsection 7.2 (ACH Operators Establish Settlement Procedures) – Clarifies that the settlement procedures established by an ACH Operator apply to the entries processed by that ACH Operator.
- Article Seven, Subsection 7.3 (Settlement) – Clarifies that an ACH Operator is responsible for effecting settlement for entries transmitted through such ACH Operator.
- Article Eight, Subsection 8.33 (Entry) – Modifies the definition of Entry to include any order or request for the transfer of money to or from the account of a Receiver, or a Non-Monetary Entry, that is formatted in accordance with the NACHA formatting requirements, utilizes or relies on an SEC Code, or is Transmitted pursuant to an agreement that incorporates or otherwise reference any provision, section or requirement of the Rules.
- Article Eight, Subsection 8.53 (Non-Operator Entry) – Adds a definition for Non-Operator Entry (e.g. an Entry not processed by an ACH Operator).
- Article Eight, Subsection 8.55 (On-Us Entry) – Adds a definition for an On-Us Entry (e.g. a Non-Operator Entry for which the account of the Originator and Receiver are held by the same Participating DFI).