An ACH (Electronic Payment) Primer:

How Savvy Companies Now Pay Their Bills

Author: Mary S. Schaeffer

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Course Information

Course Title: An ACH (Electronic Payment) Primer: How Savvy Companies Now Pay Their Bills

Learning Objectives:

- Identify the reasons why paying electronically benefits an organization
- Pinpoint issues to be considered when setting up an electronic payment program
- Create a basic ACH payment program for an organization
- Build an effective strategy for converting suppliers to the Identify effective strategies to grow your ACH payment program
- Develop an effective strategy for converting suppliers to the program
- Understand the different types of payment fraud currently being perpetrated
- Develop an effective strategy to combat electronic payment fraud
- Develop a Best Practice ACH payment initiative
- Avoid worst practices as well as hidden pitfalls when setting up an ACH payment program

Subject Area: Accounting

Prerequisites: None

Program Level: Overview

Program Content: Almost three-quarters of all companies now make at least a few payments electronically using the ACH. Those numbers, along with the size of those programs will only grow as organizations recognize the cost-savings and efficiencies associated with an ACH payment program. This course presents basic information the professional can use to properly set up and grow and ACH payment program. Industry expert Mary Schaeffer shows auditors, controllers, and managers exactly how to do this. She also alerts readers to the growing threat of fraud in this arena, offering advice for everyone – whether or not they are currently making electronic payments. "Everyone who does not take the proper precautions is at risk," she warns.

Advance Preparation: None

Recommended CPE Credit: 2 hours

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Chapter 1: How ACH Payments Work

Learning Objectives:

- Identify the reasons why paying electronically benefits an organization
- Pinpoint issues to be considered when setting up an electronic payment program

People who get their paycheck directly deposited into their bank account is part of the electronic payment revolution. In fact, mimicking the direct deposit terminology that most people are familiar with, NACHA (the National Automated Clearing House Association) recently named payments made electronically through the ACH "direct payments." NACHA, the Electronic Payments Association, is responsible for electronic payments that go through its local networks.

Automated Clearing House Network

The Automated Clearing House (ACH) Network is a nationwide batch-oriented electronic funds transfer system governed by NACHA. It provides for the interbank clearing of electronic payments for participating depository financial institutions. The Federal Reserve and Electronic Payments Network act as ACH operators, central clearing facilities through which financial institutions transmit or receive ACH entries.

NACHA represents more than 11,000 financial institutions through direct memberships and a network of regional payments associations, and 650 organizations through its industry councils.

ACH payments include:

- Direct deposit of payroll, Social Security and other government benefits, and tax refunds
- Direct payment of consumer bills such as mortgages, loans, utility bills, and insurance premiums
- Business-to-business (B2B) payments
- E-checks
- E-commerce payments
- Federal, state, and local tax payments

Most of what is written about electronic payments in this course will fall under the heading of B2B payments. The term electronic payments for the purpose of this course is synonymous with ACH payments.

For those readers who may want to peg their campaigns to grow their programs to some sort of a national initiative, May is Direct Deposit and Direct Payment month.

ACH Payment Growth

Nearly 14 billion automated clearing house (ACH) payments were made in 2012, according to statistics compiled by NACHA. A total of $36.9 trillion was transferred over the ACH Network in 2012, an increase of 8.76 percent over the prior year.

Interestingly, the biggest growth has come on the consumer side, as consumers embrace online bill payment options in record numbers and newer applications used primarily to collect their bill payments. Examples of this might be a bank debiting an individual's bank account for monthly mortgage or insurance payments.

Business Payments

Organizations of all sorts use the ACH Network for payments to and from trading partners, vendor payments, business-to-government tax withholdings, intra-company cash management transfers, and to exchange remittance information regarding payments.

Business-to-business (B2B) transaction categories, which enable B2B credit payments and the use of addenda records for remittance purposes, grew by 5.1 percent. Direct Deposits via ACH, another credit payment, also saw significant growth. In 2012, there were a total of 5.1 billion Direct Deposit via ACH transactions, representing a 5.4 percent increase over 2011.

The Basics: ACH Credits

An ACH credit is a payer-initiated transaction. The payer instructs its financial institution to electronically transmit the payment through the ACH/Federal Reserve network to the payee's bank account. Typically the funds are available the day after the transaction takes place. This eliminates all delays associated with mail and processing float.

The most common examples of this are direct deposit of payroll, where the employer is the payer and the employee the payee. One of the biggest users of this type of payment vehicle is the Federal government when it direct deposits Social Security payments. In this case the recipients are the payees. It should be noted that starting in 2013, anyone signing up to receive Social Security benefits will have to receive them electronically. The Feds are starting to get out of the paper check business.

In recent years, businesses of all sorts have started making payments using the ACH instead of paper checks or in some cases, wire transfers. Because of the connection to direct deposit, this has led some to refer to this type of payment as a 'direct payment.'

The Basics: ACH Debits

An ACH debit is a payee-initiated transaction. The payee instructs the payer's financial institution to electronically transmit the payment through the ACH/Federal Reserve network to the payee's bank account. Typically the funds are available the day after the transaction takes place. These transactions are initiated using your bank transit and routing number and your bank account number. It is implied that you have given your consent but there is no formal verification process by the bank to ensure you have given your approval. There are new bank products just emerging that provide some protection against unauthorized debits.

The most common examples of the use of ACH debits is in the financial services sector. Some financial institutions granting mortgages will, with the payer's permission, debit the payer's bank account for the agreed amount on an agreed upon date each month. Sometimes there is a slight reduction in the mortgage rate in exchange for this arrangement. The insurance industry has also used this approach with some of its insurance products.

This payment vehicle has also migrated to the business community. Some states collect their sales and use tax using this approach. A few organizations make intercompany transfers this way. In a couple of rare instances ACH debits are negotiated as part of the terms and conditions in a sales agreement. While we never expect to see ACH debits play a prominent part in the payment world, they are a vehicle that will play a continuing role. It is critical that every professional involved with payments understand them because they are used by fraudsters in growing numbers.

Issues to Consider

As you are probably painfully aware, checks are costly and create lots of problems. Electronic payments are definitely cheaper—roughly 20 cents an item by most estimates—and create far fewer problems. Here are a few considerations to take into account when deciding to make the move away from paper:

- Float. Since the payment you initiate today will hit the payee's bank tomorrow, the mail and processing float are squeezed out of the equation. Some who find this objectionable, despite all the other savings, have renegotiated payment terms with their suppliers to make the transactions float neutral. For the most part, the float period is split. Since most people believe that mail and processing float is about five days, adding two or three days to the payment terms is generally considered acceptable. However, this should be discussed with suppliers rather than taken arbitrarily.

- Bank account reconciliations. Since there should be no outstanding items, bank account reconciliations should be easier for these items.

- Fraud issues. While a move to electronic payments will certainly reduce check fraud problems, it will not completely eliminate all payment fraud concerns. It would be naive to think that all fraud considerations would disappear. ACH fraud currently is at a much lower level than check fraud, but it does exist. Steps you can and should take to guard against ACH fraud are discussed in Chapter 17. Note that some of these steps should be taken whether your organization makes electronic payments or not.

- Strong up-front controls. Since there is no signature on the payment, strong up-front controls are crucial as there is no signer "available" to catch errors. While it is true that signers shouldn't be catching mistakes, in reality they often do.

- Escheat. Since there are no un-cashed checks, there are no escheat issues related to payments made this way.

- Vendors. There are vendor issues related to cash application. While one would think that vendors would be clamoring to be paid electronically, this has not turned out to be the case. Apparently some systems have trouble applying cash received electronically. Thus, some of your vendors may be reluctant to accept payments electronically despite the obvious benefits.

- Staff reluctance to change. As with any new initiative, expect to find some of your staff dragging their feet and complaining about the change. It goes with the territory.

- Headcount. The reality is once your program is up and running, you'll need fewer people to process payments, if you've managed to convert a significant portion of your vendors to the process. However, don't jump the gun. Getting vendors on board to the electronic payment program will take time and effort. Thus, initially you may need more people if you want to make one big push. This is one of the reasons many organizations slowly add vendors to their electronic payment program.

How to Avoid ACH Payment Conversion Nightmares

If you do not execute your ACH payment conversion carefully, you could end up dooming the program before it has a chance to start. Learning from others' mishaps is one way to avoid making the same mistakes yourself. Unfortunately, often people are not willing to share their horror stories. One such story is about an organization that had a terrible time converting vendors to receive ACH payment. Some of the issues that could have been handled better include:

1) Master vendor file. Not cleaning up the vendor database before requesting (actually demanding) that the vendors convert from check payments to ACH can lead to huge problems. The example organization had multiple active vendor codes in the system for the same vendors. It used SAP with one company code for multiple business areas.

A huge disadvantage to the one-code-for-multiple-areas method is that when a payment proposal is done for one business area, the vendor will rarely realize it was only for one business area, not the entire company. If, for example, vendor code 123 is in the proposal for business area ABC, when business area DEF runs its proposal, vendor code 123 will be blocked to them. SAP does not give you an error message or any type of notice that it has blocked certain vendors—you just have to be on top of it to know if you're expecting a vendor to be paid and it doesn't come up in your proposal.

That's a long-winded explanation, but it is the primary reason the example organization had so many active duplicate vendor codes. In addition, the method used for converting vendors to ACH was not very vendor friendly.

For example, Vendor ABC sells raw materials to eight of the firm's divisions. It had eight different vendor codes set up in SAP due to the blocking issue just described. A list of all of vendors and their addresses was obtained from SAP by business area. So the company had eight different lists, each one showing ABC once. As each list was processed separately, ABC received eight different requests (and threats) to send their banking information or else! A cutoff date was named after which the company would no longer be issuing checks to them.

Here's the kicker. ABC Company would say, "Mm, sounds pretty good, sign me up!" and fill out one of the forms. After all, it only has one bank account. ABC would send along a copy of the company W-9, which was also requested (not because it was needed for the ACH conversion, but to update records). This was probably the only thing the firm did right. The vendor would send back one form and one W-9. Each form had the vendor's number on it. The company only updated the one vendor number that was on the one form ABC sent back—not all eight vendor numbers. Therefore, one vendor code was changed to ACH, the other seven received a threatening second request letter (which they ignored since they thought they had already responded) and continued to receive check payments until the company put them on payment block and quit paying them altogether. You can imagine how well this went over.

2) Getting accurate bank information. Another big mistake was not requiring a copy of a canceled check to enter the ACH information from. The company accepted handwritten forms. This is a huge no-no. First, people get ACH payments and wire transfers confused. To the vendors, they are one and the same. To the banks, they are not. Many people gave the American Bankers Association (ABA) routing number for wire transfers and the ACH payment was rejected which wreaked havoc on the company's computer systems. The staff spent many frustrating hours on phone calls trying to explain the difference to people only to wind up calling their banks in the end anyway.

3) Fraud potential. The company was also often fearful of the following scenario—one that could be avoided simply by asking for that voided check. After setting a vendor up on ACH payment (from a handwritten form with an illegible signature), the vendor would call and ask why the company had stopped paying them. After further investigation, the staff would discover that the account the company was sending money to did not belong to the company at all, but to a disgruntled mail clerk who had left the company shortly after completing the form with an offshore account set up in an untraceable alias. You should insist on getting a voided check.

4) Vendor setups. Another mistake was that after going through all this work to clean up vendors, change accounts, and update records, the company did not centralize vendor setups to one individual who was responsible for verifying and maintaining data. It simply changed its procedures to require all new vendors to accept ACH payment in order to be set up in the system, but the procedure was not enforced.

Vendors that had been blocked for noncompliance were gradually unblocked, and the amount of checks issued began to rise. Without one central department being held accountable for the integrity of the vendor database, the entire effort of the ACH conversion project was completely wasted.

While it is never possible to completely eliminate all problems, use the procedures that follow will make a big dent in the problems you will encounter when starting an ACH payment program—especially if you insist that all your vendors participate:

5) Get banking data from a voided check—not a handwritten form.

6) Request an up-to-date W-9 at the same time.

7) Start your electronic payment program with a small group so you can make adjustments to your program before rolling it out to your entire vendor constituency.

8) Before you demand that all vendors accept payments electronically, make sure all your systems and processes are working 100%.

9) If one vendor is in your master vendor file more than once, make sure those entries are linked for purposes of updating with banking information.

Use ACH Payments to Solve the Rush Check Problem

A rush check (also referred to as an ASAP check) is any check produced outside the normal check production cycle. Organizations that run their checks from a mainframe computer are often forced to either use a typewriter or handwrite a check that is produced outside the normal cycle. Even those that print them on a personal computer have issues with rush checks.

Rush checks not only disrupt the work flow in accounts payable, making the department less efficient, they also open the door to fraud and duplicate payments. An inordinate amount of duplicate payments are checks that were rush checks. This is due to the fact that sometimes the check has been cut and is somewhere in the system, waiting for an approval, a signature, or to be mailed. Inevitably, both checks get cashed—and rarely is the second returned without the prompting of a duplicate payment audit.

The size of the problem will vary at different organizations depending on how good invoice processing procedures are and how accommodating the organization is toward requests for rush checks. Some organizations dig their heels in issuing rush payments only in cases of dire emergency while others allow them under almost any circumstance.

ACH payments provide a very real solution to the rush check dilemma. By adopting a policy that all rush payments requests that are honored will be fulfilled with an ACH payment, a company solves many of the problems caused by rush checks while simultaneously introducing new vendors to the electronic payment process. The vendor demanding the rush check will have good funds in its account before it would write a check. Often once a vendor experiences the benefits of ACH payments, it will willingly sign up for that type of payment in the future. It can be a win-win for both parties, turning a bad situation into one that improves supplier relations.

Don't Overlook the Remittance Information Issue

On the face of it, you'd think every supplier would be clamoring for electronic payments. Yet, some refuse to accept them. While at first this seems counterintuitive, there is a good reason for this reluctance. Their cash application folks have difficulty applying cash without that all important remittance information. If this hurdle can be overcome, many are all too happy to get onboard accepting electronic payments.

Create a separate e-mail with all the remittance information and e-mail it to the appropriate accounts receivable or cash application person at your vendors. This will provide them the information needed to apply cash correctly and should remove what is hopefully the last obstacle to their accepting electronic payments. What's more, if you are able to provide this information a day or two in advance of the payment, it might also help with their short-term cash forecasting—another side benefit.

If that's not possible, consider mailing the remittance information after the fact. While this is better than nothing, it does take away some of the cost savings associated with the move to electronic payments.

Ignore the issue of remittance advices and the number of suppliers willing to accept ACH payments will be lower than it might be otherwise. Even if your vendor is willing to accept payments electronically without remittance information, you are putting your organization at the mercy of their cash application person. Typically, without other instructions, they will apply whatever cash comes in to the oldest outstanding invoice. This may not be what you intended. For example it could be a disputed invoice that you have no intention of paying. Hence, it is critical that remittance information be included so the supplier knows precisely what you intended to pay with.

Review Questions

1) Who initiates and ACH credit transaction?

A. Payor initiates the transaction
B. Payee initiates the transaction
C. Bank initiates the transaction
D. Either the payor or the payee initiates the transaction

2) How should a company get banking information from a vendor to set them up for ACH payments?

A. It doesn’t really matter as long as you get the information
B. Verbally over the phone
C. From a canceled or voided check
D. In a handwritten note

Review Questions Explained

1) Who initiates and ACH credit transaction?

A. Correct. Payor initiates the transaction
B. Incorrect. The payee does not initiate the transaction when a credit is involved.
C. Incorrect. The bank must wait for instructions in order to process any ACH transaction
D. Incorrect. Only the payor can initiate the transaction

2) How should a company get banking information from a vendor to set them up for ACH payments?

A. Incorrect. It most definitely matters and if standardized practices are not followed, errors will creep in.
B. Incorrect. Getting information verbally over the phone is likely to result in errors, transpositions and misunderstandings.
C. Correct. By getting the information from a canceled or voided check, there is no chance for misinterpretation.
D. Incorrect. Getting the information in a handwritten note is asking for trouble, especially if the handwriting is not perfect.

Chapter 2: How to Start an ACH Payment Program

Learning Objectives:

- Create a basic ACH payment program for an organization
- Build an effective strategy for converting suppliers to the program

New ACH payment programs will be started for a variety of any one of the following reasons:

- Someone in accounts payable or treasury recommends the vehicle. It can take several go-rounds before approval to start is received.
- Someone in management hears a talk on the benefits and comes back and orders accounts payable to start paying all vendors electronically.
- A key supplier asks your organization to pay it electronically.
- A key supplier demands you pay electronically if you want to continue buying from the company.

Benefits

The advantages of electronic payments are numerous. Lower cost typically heads the list of reasons organizations make the move. ACH payments are estimated to cost about 20 cents apiece while checks can range in cost from $3 to $20 (and sometimes more), depending on the process and efficiency of the issuing organization. Additional advantages include:

- Elimination of mailing costs.
- Supplier convenience through eliminating the check-cashing function.
- Simpler cash application process for the vendor when an e-mail with the pertinent details is sent along with the payment.
- No un-cashed checks means escheat issues are eliminated.
- Exception handling is minimized as errors are reduced.
- Accounting issues are also reduced.

The First Step

As with any high-level project, management buy-in is essential. Without management support, your program will fall apart as the complainers in your organization start whining. Even better than management support is a management evangelist, who fervently backs the program.

The cost savings associated with a program is a good way to get management support, as any savings offered by vendors for paying electronically go right to the bottom line. In fact, some organizations have used the program (at least initially) as a vendor benefit and asked for small discounts as a reward for paying electronically. Whether you will be able to do this will depend in large part on whether it is standard in your industry.

If you can’t get support for the program, wait for the right opportunity. This might be when management calls for downsizing. Another opportunity might arise when a problem crops up that would not have occurred if you had the program in place.

It is also a good idea to make your bank your partner in this endeavor. As you launch the program, you will depend on the bank a great deal. Don't overlook this valuable resource.

Get input for your program from all affected parties, including likely critics. If you include them up front, they are less likely to cause problems down the road. In fact, if they feel they are part of the program, they may even advocate for it among other complainers.

Realize that it will be necessary to spend quite a bit of time coordinating the program at the start. Make a realistic assessment regarding information technology (IT) resources. Do you have the capability in-house, or will it be necessary to hire an outside service to get your program up and running? Even if the resources are available in house, will you be able to get an adequate allocation? What's more, if you get the allocation, do you expect the IT staff to be pulled off your project as more pressing projects arise?

Don't underestimate the effect instituting electronic payments will have on your staff. Getting vendors up and running takes time. Don't try to convert all your suppliers at once. Carefully estimate just how many vendors can be converted at one time. Better to have too few candidates in your first offering than too many.

Develop policies and procedures on how to make electronic payments from the accounts payable department. Make sure these processes are integrated into your entire payment process. This will mean involving purchasing and other accounting units. Some adjustments may have to be made in the accounting software to ensure that purchase orders (Pos) are canceled and checks are not cut when the payment is initiated.

A Good Starting Point

It's best to iron out the kinks in-house before testing the process on valued suppliers. You might require all payments to employees be made using the ACH. Be aware that while it is possible to do this for T&E reimbursements, some states do not allow organizations to mandate electronic payments for paychecks. Make sure to check your state requirements before trying this with payroll.

Perhaps some of your employees have been asking to be reimbursed electronically. If you want to start with a very small group to ensure the program is working, ask them to be your beta candidates.

To reduce calls from vendors or employees who don't know what the payments are for or don't realize they received it, provide e-mail notification capability, which may be linked to the vendor master file. This will mean getting e-mail addresses and keeping that file updated.

Third-Party Participation

When you are ready to invite participation, review your vendor listings. You might begin with those suppliers who have requested electronic payment in the past. You won't have to hold their hands as you walk them through the process. In fact, they may offer you some tips.

You might also consider those suppliers already being paid by wire transfer. They are accustomed to electronic payments, and the switch from wire to ACH will save your firm from paying wire transfer fees. Some organizations initiate wires outside the accounts payable process. Depending on your accounting system, ACH may tighten controls as all payments will go through one process instead of two.

When you are confident that you have everything under control, it's time to turn your attention to your suppliers. Once you are satisfied with the retooled program, roll it out to a small group. Get feedback again, and if necessary tweak the program to meet any objections and suggestions.

Make it easy for them to sign up. Send a letter to your targeted vendors including an ACH authorization form. Once again, start with a targeted list. The reason for this is simple: The response rate might be higher than you expect. If discounts are available from vendors for electronic payments, you will want to work with purchasing to ensure that you receive all you can.

Replacing Wire Transfers with ACH Payments

For organizations that pay many obligations with wire transfers, the ACH alternative will save them a bit of money. This savings is often an added incentive to start such a program. Should you decide to replace wires with ACH, do not overlook the issue of availability of funds. Discuss it with each payee if you think it will be an issue. Most wires result in funds being available immediately, on the day the wire, for the recipient.

If you use the ACH, typically the funds are available the following day, although they should post on the day the ACH is done. This is similar to a check that might be deposited on one day but not be good funds for two or three days. If this timing is important, say in the payoff of a loan, you might have to initiate the ACH a day or two earlier. However, if the only concern is the date the funds hit the recipient's account, then there is no issue.

Before Rolling Out to Your Entire List

Once you have a number of vendors enrolled, take a step back. Don't assume everything is going well; inquire if it is. Send an e-mail with your name and phone number to vendors included in the program. It is important to identify potential problems early in the game, when it is easier to fix them and not too many potential payees have been turned off by your process.

You should also anticipate problems. Talk to your peers at other companies and see what their experiences were. Here's a list of some problems encountered by professionals with active programs:

- Incorrect bank account information from suppliers
- Input errors
- Bank mergers resulting in changes to a bank's routing number
- Vendors failing to notify customers when closing or changing bank accounts
- ACH kickback notices not received
- Vendors not receiving e-mails with payment information

Vendor Participation

Identify what payments you want to include. If there is any chance that you will want to pay someone at some point with a purchase card (p-card), do not invite the vendor to participate in your electronic payment program. Here's why. When vendors receive a payment via p-cards, they must pay the bank a processing fee. This typically is between 2 and 3% unless the vendor is very small, in which case it might be higher.

Vendors that receive payments electronically will be extremely reluctant to accept credit card payments in lieu of electronic payments. Once this bell is rung, it is almost impossible to un-ring it. The only possible exception would be for very small payments, for which p-cards are ideal.

Break your target vendor list down into where you want to start and those payments and vendors who you might eventually want to include once the program is successful. Be aware that as word spreads, you may get requests to join your program. Remember also that if you are going to ask for a pricing discount, a small rebate or renegotiated payment terms, you will need to include purchasing, if that is the department that negotiates such issues with suppliers. This is a good way to improve relations with purchasing if they are frayed.

Also, once you get started, you may find that vendors who did not initially want to participate in your program will change their minds. Alternatively, another customer may have demanded they accept payments electronically and once they started, they find they prefer payments in this manner.

Be careful how you roll out your e-payment program. If you try to enroll too many vendors in at once, the program may blow up as you don't have adequate staff to handle it.

Document, Document, Document

When you introduce an e-payment program, your procedures will change. Update your policies and procedures manual, and share this information with all affected parties. If you have your procedures posted on your intranet site, add the new e-payment processes.

Not only will you have to write new procedures for the e-payment program, you may have to revise other sections that are affected by your new process. Do not overlook these.

This might also be a good time to review some of your forms used in the payment process and bring them up-to-date.

Train, Train, Train

With your new procedures in place, you will need to make sure the entire staff knows the new process. Never assume that the information is too basic. The accounts payable staff as well as anyone affected by the process, perhaps including purchasing and suppliers enrolled in the program, will need some training.

Without training, you could doom the program. Should one vendor have a bad experience, even if it was entirely the vendor's fault, you will have a hard time convincing that company to continue to participate in your program.

Once the program is up and running and you are ready to invite every vendor to participate, include an e-payment enrollment form with your new vendor pack and a welcome letter. Do not forget to ask for a voided check so you can verify the account number as well as the transit and routing numbers. Your vendor may offer a deposit ticket instead of the voided check. This will work most of the time. However, a few banks do not include the requisite information on their deposit tickets. Thus, if at all possible, get the voided check.

Don't Overlook Metrics

Most organizations adopt an e-payment program at least partially because of the cost savings associated with the process. Having promised management certain savings, it's a good idea to go back periodically and measure those savings to make sure the program is producing. It is also a good idea to do this so the next time you make a proposal and are asked about the savings related to ACH payments, you will not be blindsided.

The savings are not always that easily to quantify. At a minimum, they should include:

- Postage savings of not having to mail checks
- Check printing costs
- Check clearing costs at the bank
- Any discounts or rebates received from vendors for paying electronically
- Any headcount reductions that may occur as a result
- Time savings resulting from not having to process checks

Other savings may be unique to your organization. Include them. Of course, since you are including all the check-related costs, you will need to offset your savings with the cost the bank charges you for ACH payments.

Vendor Satisfaction Survey

Periodically, perhaps as part of a larger vendor satisfaction survey, ask participants in your program about their experiences. Take the results seriously, and tweak your program if the survey results indicate a weakness in your approach. Do not overlook the opportunity to ask participants for suggestions.

It is hoped that they will share with you approaches taken by other companies that work well—techniques you can incorporate into your own program. Use the survey to learn from your own mistakes as well as the success of others. There is absolutely no reason why if you see a good idea at another company you cannot bring it home and make it your own.

Concluding Thoughts

According to a recent Accounts Payable Now & Tomorrow survey, 73% of all organizations now make at least a few ACH payments. This is up drastically from 34% five years ago. Of the participants, 91% said they expected to be making payments through the ACH within five years. The number is probably understated. If you do not currently have an ACH program, begin investigating one. It's only a matter of time before the market will require it of you.

Review Questions

1) Which of the following is a benefit of paying electronically through the ACH?

A. Mailing costs are increased
B. Less unclaimed property reporting and remitting
C. Exception handling increased
D. Staff in purchasing can be reduced

2) When you start an ACH program, which of the following steps should you take?

A. Wait until the next annual update, to include information in your policy and procedures manual
B. Wait until you have all the kinks worked out before training any processors
C. Document every step in the procedure so everyone knows what to do
D. Identify early participants based on how long they've been doing business with the company

Review Questions Explained

1) Which of the following is a benefit of paying electronically through the ACH?

A. Incorrect. Mailing costs are not increased, they are decreased.
B. Correct. Less unclaimed property reporting and remitting is one of the benefits as there are no un-cashed checks to chase and report.
C. Incorrect. Exception handling is not affected by an move to ACH.
D. Incorrect. Staff in purchasing is also not affected by a move to ACH.

2) When you start an ACH program, which of the following steps should you take?

A. Incorrect. By waiting until the next annual update, to include information in your policy and procedures manual, you are almost guaranteeing there will be mistakes in that time period.
B. Incorrect. By wait until you have all the kinks worked out before training any processors, your processors will have no guidelines and will inevitably make more mistakes than if they had a reference guide to check.
C. Correct. By documenting every step in the procedure so everyone knows what to do, you minimize the opportunities for the staff to make mistakes.
D. Incorrect. Identifying early participants based on how long they’ve been doing business with the company is a terrible way to select participants in your early ACH programs. You want to focus on those who understand ACH and will be sympathetic if something goes wrong. These parties may or may not be those who you’ve done business with for some time.

Chapter 3: How to Expand an ACH Payment Program

Learning Objectives:

- Identify effective strategies to grow your ACH payment program
- Develop an effective strategy for converting suppliers to the program

You're convinced and you've even managed to get management on board. You all agree that paying electronically makes a lot of sense—both for you and for the suppliers you pay. Having won the internal battle, you now face your next challenge: getting an appropriate level of participation in the program. Not only does the program make financial sense for the company, but you've put your reputation on the line. How are you going to deliver?

Market Status

ACH payments alleviate many of the problems associated with paper checks. They are among the most cost-efficient payment mechanisms currently available. This is one of those issues that is actually win-win for both parties. Unlike other matters in business, where one party gains at the expense of the other, the automated clearing house (ACH) payment mechanism really does benefit both parties.

A few savvy vendors in aggressive markets will use ACH to develop a competitive advantage for their products. They do this in several ways. One technique currently in use is to offer slight pricing discounts or rebates to those customers who agree to pay them electronically. In cutthroat markets, this could give one supplier an advantage over another.

Another technique used is to renegotiate payment terms to make the transaction float neutral. Until recently, the request for the renegotiated payment terms came almost entirely from the customer. Now, in an attempt to entice participation, a few vendors are voluntarily offering slightly extended terms.

Don't think that because the vendor hasn't offered the pricing discount or renegotiated payment terms, they aren't available. Ask. Often vendors will grant them if asked; if not asked, however, they stay mum on the subject.

Methods to Grow Your ACH Program

Some strategies to raise supplier participation in your program follow.

- Don't bite off more than you can chew. Begin by figuring out how many suppliers you could comfortably convert from paper to electronic payment in a given month. There is a good reason to do this. If the response to your first offering is overwhelming, you may not be able to process in a timely manner everyone who expresses interest. The worst thing you could do for your new electronic initiative is not deliver as promised. If you fail with a particular supplier the first time out, it is going to be a long time before you get that supplier's agreement again.

- Start slow with a test group. These should be suppliers that either are already accepting payments electronically and/or those with whom you have a really good relationship—those vendors that won't be turned off if the first pass doesn't go as smoothly as you'd like. Vendors that have solicited you to pay them electronically make excellent candidates for your test group. Since they've requested you pay them electronically, they are more likely to be understanding if things go awry in the beginning.

- Roll out your program. Once you've figured out what you can reasonably handle and your processes are working smoothly, send out a mass mailing to targeted suppliers you want to pay electronically. You might, for example, exclude those suppliers you prefer to pay using the purchase card (p-card). Not everyone you solicit will accept your electronic invitation. So, if you can handle 100 conversions a month, send your initial solicitation to 200 or 300. Keep running your monthly solicitations until you have gone through your entire targeted market.

- Get on the phone. Once you've finished your initial campaign, you are ready to take the next, more aggressive, step. You'll need to go after the laggards who did not have the good sense to sign up for your electronic payment initiative. Begin by outlining all the benefits of receiving payments electronically. Once you have the list firmly in hand, pick up the phone and start calling. Sometimes all it takes is a simple phone call and a little conversation to get the ball rolling. At other times, the vendor will have a real objection; a real an reason electronic payment cannot be accepted. Address these issues if you can. If you can't, note what they are for future reference.

- If you can't get in the front door, try climbing in through a window. Now you have to get sneaky. The next time one of your nonparticipating vendors calls looking for a payment that was needed yesterday, take advantage of the opportunity. Even if the delay is entirely your company's fault, suggest that you can pay electronically today or tomorrow (whatever your schedule allows) but will not be able to draw a check and mail it until…. Point out that given mail time, it might take a week or more until the vendor has the funds in its account, but if you pay electronically, it can have good funds the next day.

- The door is never completely closed. After six months or even perhaps a year, revisit the issue with those who have not signed up. More often than not you will find that a vendor who did not have the capability when it was first suggested has upgraded, and you will be able to enroll a portion of this group.

- Roll up your sleeves and get ready to work. Now it's time to address the "problem children," the companies that have real operational issues that prevent them from accepting electronic payments. Go back to the notes you took when making your initial phone calls. Categorize them and identify the most common issues. Then look for solutions to those problems. See if any of the vendors you are currently paying electronically had these issues. If they did, find out how they solved the problem. Armed with this information, you are prepared to provide your suppliers with a potential solution. If the solutions you offer have some value, you may not only add the vendor to your electronic payment clients, but you will also have enhanced the relationship with that vendor—something purchasing should appreciate!

- Take a real hard-ball approach. This tactic won't work in every situation (especially if you are dealing with some 800-pound gorilla suppliers), but it will work on occasion. Levy a fee on those vendors who refuse to be paid electronically. Charge them $25 for every check you cut to them. (Note: Depending on the relationship you are trying to foster with your suppliers, this may not be a tactic you and your firm chose to employ. Accounts payable professionals should do this only with management's blessing and purchasing's knowledge. Should a key vendor complain, or, worse, halt deliveries, the repercussions from these two groups will not be pretty if they were not in the loop on this decision.)

- Don't overlook your Web site. Publish ACH information on the password protected supplier portal of your Web site, if you have one. Occasionally a vendor you might not have approached will want to participate. Make it easy. Also, if you are going to take this approach, include your vendor enrollment form on the site. Use this approach only if you are willing to include all vendors in the program. Otherwise, you may find your p-card vendors signing up for the program—and there goes your rebate.

- Vendor satisfaction survey. Include a question in your vendor satisfaction survey asking if the supplier would like to be paid electronically. Of course, do this only if you are looking to include that vendor in your program.

- Take advantage of those "where's my money" calls. When the vendor calls looking to ensure payment, (you know, those annoying calls vendors make to ensure you have the invoice and will be paying it on time) point out the benefits of receiving payments electronically and try and sign them up.

- Use your internal e-mail to promote the program. Take a page from the marketers' book. Develop a tag line for your e-mail messages that you send vendors. It could say something like "Interested in receiving your payments from us faster? Ask me about our electronic payment program."

- Cold call. Don't overlook the phone as a potential tool. Make sure you target the right person. Often the pitches go to the salesperson, who, in many cases, has little interest in the payment aspects of the transaction. Take your list of targeted vendors and start calling their accounts receivable or credit manager. These are the people who are likely to be interested in receiving payments electronically. If you are making the pitch on the basis of financial savings, you could also try the chief financial officer, controller, or treasurer.

- Universal Payment Identification Code (UPIC). Occasionally you will run into suppliers who are reluctant to share banking information for fear of fraud. Suggest they get a UPIC. UPICs are discussed toward the end of this chapter.

Renegotiating Payment Terms

Much has been written about renegotiating payment terms in this book. Often when the topic is raised, management is reluctant because they perceive that they will lose the float benefits. Companies that want to use this new technology yet are not willing to give up the few extra days of "float" can renegotiate their payment terms with vendors to make the transaction float neutral. This way neither party gains or loses by the transition to the new payment methodology.

When payments are made electronically, the funds get into the supplier's bank account immediately and generally the vendor has use of good funds one day later. This is typically several days sooner than if the check had gone through the traditional printing and mailing cycle. Recognizing this fact, some companies use this information to entice vendors to accept payments electronically.

Should you take this tack? In an ideal world the answer is, of course yes. But if vendors refuse to renegotiate the terms, you may end up continuing paying them with paper checks. So the real answer is: It depends. If your company's primary goal is to get rid of the checks, then the answer is to tread lightly on the float issue. If, however, cash flow is an issue for your firm, then you may have to rethink how you address the terms question. Accounts payable managers should not make this decision in a vacuum. Management input is required when deciding how important float is in this equation.

Pricing Discounts

Occasionally some suppliers will offer small pricing discounts or rebates to their customers who agree to pay them electronically. This is the best of all worlds for customers. They get to pay with the least expensive payment mechanism while simultaneously getting a price reduction or rebate—both of which effectively increase the bottom line. The offer of such savings has been more than enough to convince quite a few organizations to convert to electronic payments.

Like discounts offered for early payments, these incentives should be viewed positively and taken if at all feasible, assuming, of course, that they make financial sense.

Improved Terms versus Pricing Discounts

Generally speaking, the improved payment terms offered to make a transaction float neutral translates into two or three days added to the terms. Occasionally, if a vendor is very interested in getting paid electronically, it might offer an additional five days to make the transaction float neutral.

Pricing discounts, however, will generally be some fraction of 1%. Again, this is not a huge amount, unless you are talking about large invoices. However, it is found money that goes straight to the bottom line.

Although you should do the math if you are doubtful, generally speaking, pricing discounts or rebates should be taken, if offered, before the slightly extended payment terms.

If approaching the vendor to ask for an incentive, start with the pricing discount and then move on to the renegotiated terms to make the transaction float neutral.

Universal Payment Identification Code

Even in this day and age, you will occasionally run into vendors who refuse to give you their bank account numbers so you can pay them electronically. They say they are concerned about their banking information being used fraudulently. Given the general concern about sharing banking information, it became apparent awhile back that a universal intermediary was needed. This was the genesis of UPIC.

A UPIC is a banking address used to receive electronic credit payments. A UPIC acts exactly like a bank account number; however, the UPIC protects sensitive banking information, that is, the bank account number and the bank's routing/transit number. The UPIC masks these numbers. Only credits to an account can be initiated with a UPIC. All debits are blocked, increasing security and control. Thus, a crook could not issue an ACH debit, write a check, or issue a demand draft.

If you are wondering if the UPIC can be used with wire transfers, the answer, at least for the present, is no. Initially the UPIC may be used only in place of ACH credits.

Getting Started

If your vendors need instructions on how to get started, direct them to their bank. UPICs can be obtained from a participating bank. Most major banks will be able to facilitate this transaction. Contact your customer relationship manager or branch manager to find out if the bank issues UPICs.

It does not take long for the UPIC to be activated. Generally 24 hours after the application, the number will be live. It should be communicated with the universal routing and transit number (URT) for the bank. To be certain your vendor gets this right, the bank providing the UPIC should verify the URT.

Tried and Tested Strategies That Convinced More Suppliers to Sign up for ACH Payments

The reasons for switching from paper checks to ACH payments are many. Cost, efficiency, minimization of unclaimed property issues and cash flow planning are just a few. Despite the recognized benefits to both parties, there is still some reluctance by many suppliers to accept electronic payments. AP Now recently asked readers of its free weekly e-zine who've been successful getting vendors to sign up for ACH how they persuaded them to do so. Here are a few of the better suggestions.

The Payment Frequency Issue

Perhaps the best way to get vendors on board is to pay less frequently with checks than with ACH. That's the strategy used by quite a few of AP Now's readers. Here are a few of their comments on implementing this tactic.

- To encourage ACH, checks were cut only twice monthly whereas we did ACH daily.
- Have quicker payment terms for those vendors that accept ACH payments.
- We encourage our vendors to give us a discount and be paid by ACH. We pay these vendors on a daily basis. Otherwise, they are paid once per week.

The Benefits Approach

Quite a few companies convince vendors by simply pointing out the benefits. Here's how a few or our readers addressed the issue.

- We just let them know that by accepting ACH payments, they get paid faster and with more accuracy. No more checks lost in the mail, having to void and re-issue checks, no more phone calls from vendors looking for check payments and being told they are in the mail. ACH are easier to provide proof of payment and to validate taking early pay discounts.
- We have stressed that the time it will take for the vendor to actually receive funds will be decreased by at least a week. Between mailing the checks, taking the deposit to the bank and waiting for the check to clear. If we send an ACH, they will have funds in their account within two business days.
- We were struck by a major tornado last April. Our facilities were not impacted but unfortunately several of our vendors' physical locations were. In addition to that, during the days after the tornado, mail service was slow, if available at all in some locations. Fortunately, many of our vendors had previously signed up for ACH and we were able to continue making payments to them during this difficult time. We have been able to use this as a "plus" for ACH to convince vendors who were not signed up for ACH to do so.

The Lost Checks Opportunity

A number of readers took advantage of checks lost either in the mail or by vendors to press for ACH. Here's a look at how a few of them handle the matter.

- We charge a replacement fee for lost checks unless the vendor has submitted an ACH request for future checks.
- Whenever a vendor calls to have a check voided and re-issued, we send them a form to sign up for ACH.
- Our company doesn't replace lost checks unless the vendor submits an ACH request.

A Helping Hand from Purchasing

Increasingly accounts payable's activities overlap with other departments, especially purchasing. Here's how two of readers recruited other departments to help.

- We encouraged the purchasing department, travel, premises (anyone engaging vendors to put ACH on the table as part of their negotiations). We managed to get some nice discount terms in the bargain.
- One of the strategies that our AP department implemented involves working in conjunction with our contracting team so that when it is time to renew our vendor price agreements, switching to electronic payment is part of the new contract.

Addressing the Remittance Information Issue

One of the biggest problems with getting vendors on board with electronic payments has to do with getting them the remittance information. Here's how two of professionals addressed that problem.

- Our company has a website where all the payments are posted (for a 3 year time frame) and the website also sends an auto email when the vendor has received a payment.

- Ask for an email address where remittance information can be sent.

Additional Strategies

Even after everything discussed, there are still a few more approaches being used by our readers. The first addresses vendor complaints about early discount payments received after the discount date and the second addresses the issue with new vendors. Here are the last two suggestions.

- We have some discount vendors still receiving checks. They will contact us requesting a discount be paid back because the check was not received in time. Our comment to this is we have no control over the mail time and suggest they switch to ACH. Allowing us to pay them by ACH they will receive our payments quicker and we will no longer have a late payment issue with discounts.
- Create a form that you can email over to all new vendors with their w9. See the sample of this form on page x. Readers should verify information received on this form using contact information provided by the vendor.

Paying via the ACH is the wave of the future. It is much easier and less costly than paper checks. If you are looking for ways to increase participation (or get started) some of our proven reader tactics may be just what you need.

Review Questions

1) When starting an ACH program, which is the best approach?

A. Roll it out to your entire supplier base at once
B. Only offer it to the suppliers you do the most regular business with
C. Offer it only to the suppliers who don't send problematic invoices
D. Start small with a test group

2) Which of the following approaches can be used to entice vendors to accept ACH payments?

A. Pay electronically more frequently than by paper checks
B. Pay electronically less frequently than by paper checks
C. Pay electronically at the same frequency as by paper checks
D. Run paper checks only once a week

Review Questions Explained

1) When starting an ACH program, which is the best approach?

A. Incorrect. By rolling it out to your entire supplier base at once, you'll have a nightmare on your hands if there is a problem or your program needs tweaking.
B. Incorrect. By only offering it to the suppliers you do the most regular business with, you'll miss out on a good many vendors who would accept electronic payments.
C. Incorrect. By offering it only to the suppliers who don't send problematic invoices, you will antagonize those who wish to receive electronic payments and will miss the opportunity to grow your program.
D. Correct. By starting with a small with a test group, you'll have the opportunity to refine the program if you discover any hiccups or problematic approaches.

2) Which of the following approaches can be used to entice vendors to accept ACH payments?

A. Correct. By paying electronically more frequently than by paper checks, those suppliers who want their payments quickly will readily sign up.
B. Incorrect. By paying electronically less frequently than by paper checks, you will discourage suppliers from signing up.
C. Incorrect. Paying electronically at the same frequency as by paper checks does nothing to encourage suppliers to switch.
D. Incorrect. Running paper checks only once a week is not infrequent enough to encourage suppliers who might be reluctant to switch.

Chapter 4: How to Protect Your Organization against ACH Fraud

Learning Objectives:

- Understand the different types of payment fraud currently being perpetrated
- Develop an effective strategy to combat electronic payment fraud

ACH fraud, sometimes referred to as electronic payment fraud, is a threat every organization must deal with on a daily basis. For no organization is exempt from the prying grasps of fraudsters trying to get into any bank account they can. Making this issue even more serious than readers might be aware is the fact that some of these thefts are being masterminded by organized crime located in other countries.

Myths that Cause Problems

Fraud in the ACH world can do serious damage. Unfortunately, many organizations don't take it seriously until it's too late. They believe one of the following – all of which are FALSE:

1. We use positive pay for checks and it will protect us
2. We don't make electronic payments so we are not at risk
3. We're too big no one would dare try to steal from us
4. We're too small for anyone to be interested in us
5. Our bank will eat any losses for payments we don't authorize

Unfortunately, all of these beliefs cause trouble. If you are using positive pay with your checks, you are protected against check fraud, that's all. It does nothing to protect against ACH fraud.

Not making electronic payments means you don't make electronic payments from your own account. If you don't take the proper precautions, someone else will. So, please, don't rely on non-participation as an excuse to do nothing.

Size, also is no guarantee. Crooks will steal wherever they can. Being too small or too big offers absolutely no protection.

And finally, banks cannot afford to eat losses nor are they responsible for them legally. Do not be lulled into a false sense of security thinking that your organization is not a target. Neither non-participation in the market nor size of your organization will safeguard your accounts. Only you can do that by taking the necessary steps as discussed further in this article. But before we get to the strategies you can use, we have a quick review of the growth of this type of fraud and a very brief description of the types of ACH fraud now in play.

Electronic Payment Fraud

Without a doubt, crooks have turned to the ACH to perpetrate some sophisticated frauds. These crimes are growing and no one is immune. The crooks involved are increasingly sophisticated and the funds they steal often unrecoverable. It is important that everyone involved with payments understand the time constraints associated with identifying fraudulent ACH transactions.

As consumers, readers have 60 days to notify their financial institutions of unauthorized ACH transactions in their personal accounts. These include both ACH debits against their accounts and unauthorized ACH credits initiated from their accounts. As indicated earlier, the crooks in this arena are very smart. However, and this is a big one, anyone other than a consumer has only 24 hours to notify their bank of an unauthorized transaction.

There is no way around this. Monthly bank reconciliations won't cut it. Identifying a fraudulent transaction 30 days after the fact is too late. The money is gone. Therefore, we recommend daily account reconciliations. We also recommend using certain bank fraud prevention products, discussed in detail further on in this course.

Growth in ACH Fraud

If you go back five or more years you won't even find ACH fraud listed in any of the fraud surveys. However, that is changing and unfortunately changing quickly. Not only is fraud now included but the number of different types of ACH fraud is growing.

Thieves involved in this type of fraud are usually very smart and technologically sophisticated. They also (unfortunately) have a very good understanding of how the banking system works. They use this knowledge, along with their computer hacking skills to create new ways of getting their hands on your organization's money.

The evolution in this arena has occurred at lightning speed and is truly frightening. Just as the banking and business community develop practices and products to thwart their latest fraud, the crooks come up with another "innovation."

Types of ACH Fraud

The evolution of ACH fraud has been quite rapid. Just a few short years ago, the banking community was primarily concerned about the first type of fraud. Now, that has expanded. Today, ACH fraud can be broken into give general types as follows:

1) Representing positive pay rejects as ACH debits (unauthorized ACH debits)

2) Account hijacking also called corporate account takeover (typically via the initiation of ACH credits)

3) Reverse phishing – redirecting of electronic payments from a legitimate vendor to the fraudster

4) e-Check payments to a third party using your bank account information

5) Falsified e-mails coming from legitimate organizations containing either an attachment or a link to an illicit website. This is an alternate approach to getting information needed for an account hijacking.

There will be others as the crooks in this arena are very smart. They understand how the technology works, how the banking system operates and take advantage of this knowledge for their own benefit—at your expense.

Prevention

While you can't stop someone from trying to steal from your organization, you can make it so difficult they are not successful. What follows is a list of tactics any organization can use to prevent a fraudster from winning when trying to steal from your firm using the ACH.

1) Set up a separate computer for online banking activity only. More on this below.

2) Put ACH blocks on all accounts where ACH activity is not to be initiated; if you are paying using ACH credits, put ACH debit blocks on your accounts.

3) Put ACH filters on accounts where ACH debit activity is permitted.

4) Set up a single account for incoming wire transfers, allowing no other activity in that account. Sweep it each night into another account.

5) Do not give wire transfer information over the phone.

6) Issue refund checks from a separate account with a low-dollar limit.

7) Regular update of security and anti-virus software.

The Separate Computer Strategy

The FBI issued a press release warning businesses, municipal governments, and school districts that they are the primary targets of the newest type of electronic payment fraud. These crooks are stealing the online credentials of legitimate organizations and then using this information to steal hundreds of thousands of dollars from them. What's even worse is when the fraud unravels, unwitting individuals are left holding the bag – and these people rarely have the money to repay the stolen funds.

This separate PC should be used for online banking transactions and online banking transactions only, no exceptions. IT should not be used for surfing the web or email, as that is how key-capturing malware is sometimes surreptitiously downloaded onto the computer, providing the fraudsters with the information they need to take over an account.

Companies should also resist the temptation to let a temp use that computer. One of the easiest ways to do this is to NOT put a copy of Office (Word, Excel, PowerPoint and Access) on the machine. Also, make sure whoever uses the computer for the online banking activity, logs off as soon as they are finished. This helps remove the temptation to use the computer for a quick Internet search.

Detection

Sometimes, no matter how hard you try, an unauthorized transaction gets through. If that happens, all is not lost. If you notify the bank within 24 hours, they can retrieve your money. The following strategies are recommended for detecting unauthorized activity.

1) Perform daily bank reconciliations to identify unauthorized activity.

2) Notify the bank immediately of unauthorized activity.

Readers should note that even if they detect a fraud outside the afore-mentioned 24 hour time period, they should still contact their bank. The bank may still be able to recover some or all of the missing funds.

ACH Fraud Protection: Bank Products Currently Available

Electronic payment fraud is nasty, unsettling and expensive. What's more, every organization is a potential target, regardless of whether they make electronic payments or not. Some think, "oh, we don't participate in that arena so we're safe." That is categorically not true. What's more, organizations who are hit with an unauthorized debit have only 24 hours to alert their banks. Otherwise, they have no recourse. As the sophisticated crooks involved in electronic payment fraud crank into high gear, it is more important than ever that every professional take the appropriate steps to protect their organization. The banks can help as well. This is a look at what's currently available from the banking community.

Background

Before we discuss the products available now and being introduced this year, it is important that readers understand they need to read the product descriptions very closely. Unfortunately, it is not like positive pay (at least currently) where we can say one name and everyone knows what the product does.

Read the product description and make sure it does what you think it does. Also, make sure you understand what, if any, your obligations are regarding the use of the bank product.

Bank Products

Currently, there are four types of products either available or very close to being available. They are:

1) ACH Blocks. These are instructions given a bank to block ACH activity. You can either have all ACH activity blocked or just ACH debit activity. This needs to be done on an account by account basis. What many organizations do if they want or need to allow ACH debits is to limit that activity to one or two accounts. They then put ACH blocks on all the other accounts. If you do not want to allow any ACH debit activity, put an ACH debit block on the account.

2) ACH Filters. Should you allow ACH debits on one or more accounts, you can put a filter in place. This is a list of organizations that you have given permission to debit your account. The bank won't check the dollar amount, just the entity debiting your account. If they initiate an unauthorized transaction, the filter won't catch it. But, the filter is a big step in the right direction.

The first two products are currently available and most financial institutions offer them. The next two products are just starting to find their way into the marketplace. If your bank hasn't offered them to you, call them and ask about it.

3) ACH Payee File. This is similar to the ACH filter, but works when you initiate the payment. With this product, you supply the bank with a list of entities and people you intend to pay using ACH. Then when your list of payments comes through, if there is a payment to an entity not on your preauthorized list, the payment will not be made. This product helps protect your organization against losses from an account takeover.

4) Notification of ACH Debits. With this product, any time an ACH debit hits your account, the bank notifies you and asks if it should honor the transaction. Now, if this seems like a lot of work, consider this. Most organizations only allow a few entities to initiate ACH debits against their account. Hence, the number of phone calls should be small – unless a crook is trying to debit your account and you want those calls.

Whether we like it or not, ACH fraud continues to grow. What's more the crooks who focus on it are very sophisticated and they are continually devising new ways to steal from organizations just like yours. Thus, the protections that work today, may not address the problems that emerge next week or next year. So, it is imperative that once you create the perfect protection plan, you don't rest on your laurels. Continue to monitor the fraud situation.

ACH Fraud Case Study: It Could Happen to Any Organization—including Yours

A recent cyber-theft utilizing ACH demonstrates how important it is for all organizations to take proper security precautions. The victim was a medium-sized not-for-profit, a typical target for this type of fraud. What's more the events also show a shift in attitudes over the responsibility issue. There are some lessons to be learned for every company. Let's take a look at what happened.

The Theft

The Metropolitan Entertainment & Convention Authority, a nonprofit organization in Omaha Nebraska was hit with fraudulent ACH transactions totaling $217,000. It is believed that an employee at the organization fell for a phishing e-mail that downloaded malware software onto his computer. The employee opened an email attachment infected with a virus that stole the information. Through this software the technologically-savvy thieves were able to obtain the login and password credentials.

The cyber-crooks then add their own "hires" to the payroll. The payments went to the money mules hired through work-at-home scams. The heist was, like many others, based in an Eastern European country. Luckily, it was uncovered early and all but $70,000 was recovered.

Reaction

The organization took responsibility for the attack, surprising many in the financial community. The reason for this is illuminating. Their bank had offered several security options which the Convention Authority had passed on.

The explanation offered was that they thought the security recommendations made by the bank would be "administratively burdensome." Like many organizations they did not believe they would be victimized. The organization stepped up to the plate and did not expect its bank to compensate it for its losses.

Lessons Learned

For starters, it is imperative that every organization realize it could be a target. These thieves are known to focus their attentions on small and mid-sized businesses that are less likely to employ best fraud prevention practices. Many are unaware and others think it would never happen to them. While there have been instances of large companies being hit by ACH fraud, it is not believed that it happens often. These organizations take the proper precautions to protect themselves. Typically, their bankers also make them aware of the latest frauds. Although it does not appear to be a factor in this theft, many of these cyber-heists occur at times when offices are known to be lightly staffed. This includes the week between Christmas and New Year's day, late August etc.

Once this realization has sunk in that your organization could be a target, talk to your bankers. Ask what products they offer to protect against this insidious type of fraud. Pay close attention to the explanation of what the products actually do. There has not been much in the way of uniform protections so it is imperative that you understand what each actually does. Also ask what else they suggest. They will probably suggest, among other things, that you set up a separate computer for all your online banking activity.

This particular situation reinforces that recommendation. Your online banking should be handled on a separate computer used for NOTHING else. Few organizations follow this advice despite the fact that it is relatively inexpensive to implement. A stand-alone computer costs less than $1,000 – and if used only for online banking needs little other software. In fact, not installing other software on it will reduce the chances that someone will be tempted to use it in case of an emergency. By the way, this recommendation comes not only from those involved in the financial community but from the FBI as well.

And finally, realize that fraud is continually evolving with crooks finding new and devious ways to practice their trade. As quickly as the financial community finds ways to protect itself against the latest wave of payment fraud, the crooks find a new way to illicitly get your organization's money. This means it is imperative that every organization keep abreast of all the new types of frauds as well as the protections available to protect their funds. It also means continually revising processes to address the latest concerns. This, unfortunately, is an ongoing process, not one that is likely to remain static.

Concluding Thoughts

This is a particularly insidious type of fraud and every organization is a potential target. Not only is it important that you update your procedures and protections now, but it is critical you keep on top of this issue as crooks are continually identifying new ways to get at your account.

Review Questions

Which of the following is NOT a type of ACH fraud?

A. Account hijacking
B. Representing positive pay rejects as ACH credits
C. Representing positive pay rejects as ACH debits
D. Reverse phishing

What does an ACH filter do?

A. Stops all ACH activity
B. Allows ACH activity from pre-approved parties
C. Checks the dollar amount of transactions coming through
D. Checks on the frequency of allowable transactions

Review Questions Explained

Which of the following is NOT a type of ACH fraud?

A. Incorrect. Account hijacking is a type of ACH fraud whereby the crook takes over an account and initiates ACH credits in the company's name.
B. Correct. Representing positive pay rejects as ACH credits is not an approach used by crooks.
C. Incorrect. Representing positive pay rejects as ACH debits was the first type of ACH fraud seen in any great numbers.
D. Incorrect. Reverse phishing is a type of ACH fraud where the crook attempts to get information it needs to defraud the company.

What does an ACH filter do?

A. Incorrect. A filter does not stop all ACH activity; only certain types.
B. Correct. A filter allows ACH activity from pre-approved parties.
C. Incorrect. A filter does not check the dollar amount of transactions coming through.
D. Incorrect. A filter does not check on the frequency of allowable transactions, only allowable parties.

Chapter 5: ACH Best Practices, 'Gottchas' and Worst Practices

Learning Objectives:

- Develop a Best Practice ACH payment initiative
- Avoid worst practices as well as hidden pitfalls when setting up an ACH payment program

With the drive on everywhere to move from paper to electronic payments it is important that best practices are integrated into the new payment process. For without best practices, fraud and duplicate payments will creep back in. What follows is a list of best practices every organization should use for ACH payments

Best Practice #1: Have detailed written procedures for your ACH program and include them in the accounts payable policy and procedures manual. Don't assume your staff knows what to do.

Best Practice #2: Make sure your ACH procedures mirror you check procedures. It is critical that when processing invoices, the organization continue using the same best practices, strong internal controls and segregation of duties as is used when paying with paper checks. For if any of these steps are omitted, the organization would unintentionally weaken controls and incur other problems.

Best Practice #3: Integrate strong internal controls throughout the process. Make sure that when the ACH process is set up, no control point is overlooked. This includes making sure that appropriate segregation of duties is maintained.

Best Practice #4: Check for duplicate payments made using other payment methodologies, i.e. paper check, T&E and p-card. Ideally every organization should be paid using one and only one payment mechanism. More than occasionally, ACH payments are made outside accounts payable and the department making the payments does not employ the same rigorous practices used in accounts payable. When this happens and an invoice shows up in accounts payable, the accounts payable staff will pay it, as they cannot tell from the records that the payment has already been made.

Best Practice #5: Make sure receivers and POs are extinguished just as they would be if a paper check was the payment mechanism. This is probably the biggest potential problem spot when payments are made outside accounts payable. So, not only should the three-way match be done by whoever is making the payment, it is critical they extinguish the receiver and PO. If they don't do this, accruals and financial statements will not be accurate, as well.

Best Practice #6: Put ACH blocks on all accounts where ACH activity will not be allowed. This is something every organization should do, regardless of its participation in the electronic payment arena. For without it, an account takeover is made just a little bit easier for the crook.

Best Practice #7: Use ACH filters on those accounts where ACH debit activity will be allowed. This limits the activity to those who you have given permission to. Please note that the filter only checks for allowable parties; it does not review whether the transaction is question has been approved nor does it look at dollar amounts.

Best Practice #8: Have daily bank account reconciliations done on all accounts where ACH blocks are not used. Even better, reconcile all bank accounts on a daily basis. This ensures you are able to identify unauthorized ACH transactions within the 24 hour window, discussed earlier. The bank reconciliations have to be done anyway, so why not do them in a manner that will enable you to catch a fraud while something can still be done about it.

Best Practice #9: Use a separate PC for all your online banking activities and do not use the computer for anything else. Given the low cost of PCs, there's no reason why everyone isn't doing this.

Best Practice #10: Keep up to date on the latest information regarding fraud protection products offered by your financial institution and new frauds being perpetrated by crooks. They are getting amazingly creative. This is just one more area where it is imperative that every organization have the very latest information.

The Hidden Surprises: The 'Gotchas' That Hinder ACH Success

Speeding up cash disbursements isn't an approach most organizations willingly adopt. It's even worse when the move is unexpected—something that somehow never happens when the organization is flush with cash. (It always seems to occur when cash is tight.) Yet, that is exactly what can happen when an organization moves from checks to ACH if they don't plan ahead and make the appropriate changes in payment terms. Whenever an organization makes a change in procedures, it is crucial that thought be given to all the ramifications; the move to ACH is no exception. AP Now recently asked readers of its ezine who've made the move to ACH what issues others should expect so they can avoid fallout.

Extinguishing POs and Receivers

One of the first issues that come to mind is a surprising metric. While most checks payments are made through accounts payable, the same cannot be said for ACH payments. In a good number of organizations ACH payments are also initiated in other departments.

A very real concern is that the other departments might not extinguish the POs and open receivers opening the organization to another potential avenue for duplicate payments. We believe if others are to make ACH payments, it's crucial that adequate training be provided to those individuals. Open POs and receivers can result in duplicate payments should a second invoice be presented.

Additionally, state auditors could construe the open receiver as unclaimed property. And, if you think this is something I'm making up, let me warn you that a few organizations are fighting with state auditors over this very issue right now. Should the auditors win, they will be looking at every organization's open receivers when they come for an audit.

Open receivers can cause a misstatement of your financial records if those receivers are used for accrual purposes. If there are enough of them, the misstatement could be material. This is something no one wants hanging over them.

Obviously these issues are avoided if the organization insists that ACH payments must flow through the accounts payable system.

Setup Time Involved

"Our ERP software for the pay cycle was setup to create ACH files from these invoices but the output was nothing like what was required from the bank," reports an AP manager who requests anonymity. She notes that her staff spent endless hours completing the process to automate ACH payments. The company cut ACH payments for over 30 companies and all activity is now output to a file that is uploaded to its bank once a day. While the time savings once the process was in place is impressive, underestimating the time and effort needed to get the ACH process up and running can come back to haunt you.

This company was not home free once they had the process working, however. When they merged with another organization, they had to integrate their ACH payments with their new partners'. In this case the treasury department was involved and coordination became an issue.

Cash Flow Implications

Changing to ACH has a direct and immediate effect on cash flow. "ACHs clear the next day while your checks require mail time and deposit time at the bank, which could leave the funds in your account anywhere from three to ten days," points out an accounts payable/receivable manager.

One way to compensate for the immediate disbursal of funds, she says, would be to extend your payments to vendors a few days longer. So if you would normally cut a check on, say, May 16th wait until the 22nd to make the ACH payment. In fact, many organizations anticipate the cash flow impact and renegotiate terms with their vendors at the time they move to ACH. Those who ignore this issue will have a rude awakening the first time the ACH payments hit.

Depending on how tight the cash flow is in your organization, this could be the worst problem of all and the one with the highest visibility. If the company runs out of cash and the cause of the liquidity crisis is identified as the move to ACH without an accompanying renegotiating of payment terms, the results will not be pretty. This is *not* how any employee wants to come to the attention of upper management.

The Cash App Issue

As discussed above, the remittance advice can be problematic since there is no check stub for the vendor to see what invoices are being paid. Another manager prints off remittance advices and e-mails them to the vendors. She notes she could mail it but the payment would arrive before the remittance advice. She also points out that when vendors don't know how to apply payments, they call. And that adds more work to the accounts payable department partially offsetting the productivity gains from going electronic.

Finally, if the remittance advice is mailed, the postage cost savings goes up in smoke.

Concluding Thoughts

Use of the ACH for payment processes can result in significant savings for the organization. However, like any new process, if the full ramifications are not explored its implementation can make the process worse rather than better. By addressing the issues discussed above, you will be well on your way to avoiding an ACH implementation debacle.

A Master Vendor File Nightmare: Converting to ACH with Several Business Units

Do you have several business units doing business with the same vendor? And only one master vendor file? Not cleaning up the vendor database before requesting or, perhaps, demanding that the vendors convert from check payments to ACH can lead to huge problems. One of AP Now's readers shared the nightmares her organization encountered in this scenario.

Background

"Our organization had multiple active vendor codes in the system for the same vendors. It used SAP with one company code for multiple business areas. A huge disadvantage to the one-code-for-multiple-areas method is that when a payment proposal is done for one business area, the vendor will rarely realize it was only for one business area, not the entire company.

"If, for example, vendor code 123 is in the proposal for business area ABC, when business area DEF runs its proposal, vendor code 123 will be blocked to them. SAP doesn't give you an error message or any type of notice that it has blocked certain vendors—you just have to be on top of it to know if you're expecting a vendor to be paid and it doesn't come up in your proposal.

"That's a long-winded explanation, but it's the primary reason the example organization had so many active duplicate vendor codes," she explains.

Making the Problem Worse

In addition, the method used for converting vendors to ACH wasn't very vendor friendly. She explains, "For example, Vendor ABC sells raw materials to eight of the firm's divisions. It had eight different vendor codes set up in SAP due to the blocking issue just described. A list of all of vendors and their addresses was obtained from SAP by business area. So the company had eight different lists, each one showing ABC once. As each list was processed separately, ABC received eight different requests (and threats) to send their banking information or else! A cutoff date was named after which the company would no longer be issuing checks to them.

“Here's the kicker. ABC Company would say, "Mm, sounds pretty good, sign me up!" and fill out one of the forms. After all, it only has one bank account. ABC would send along a copy of the company W-9, which was also requested (not because it was needed for the ACH conversion, but to update records).” The writer notes that this was probably the only thing the firm did right.

The vendor would send back one form and one W-9. Each form had the vendor's number on it. The company only updated the one vendor number that was on the one form ABC sent back—not all eight vendor numbers. Therefore, one vendor code was changed to ACH, the other seven received a threatening second request letter (which they ignored since they thought they had already responded) and continued to receive check payments until the company put them on payment block and quit paying them altogether. “You can imagine how well this went over,” she concludes.

An Answer?

There is no easy answer to this problem. This is one of those situations where recognizing the problem is the first step. Ideally, identifying the issue before it occurs would be best but as anyone who has ever worked in accounts payable painfully realizes, that doesn’t always happen. Once the problem was discovered, it was time for all the business units to get together and develop a plan of action that all could live with. Clearly, since they wanted to pay everyone electronically it was just a matter of taking the letters received and going back into the system and making the necessary adjustments to the other vendor numbers. Of course, determining who was going to take on that task is another, probably not easily solved, dilemma.

Review Questions

1) How frequently should bank reconciliations be done to ensure recovery of any unauthorized transactions?

A. Weekly
B. Monthly
C. Daily
D. Never

2) Why is getting remittance detail for ACH payments to the supplier so important?

A. It is required by law
B. It is required by GAAP
C. It means more ‘where’s my money calls from suppliers
D. It facilitates cash application of the funds

Review Questions Explained

How frequently should bank reconciliations be done to ensure recovery of any unauthorized transactions?

A. Incorrect. Weekly bank reconciliations are not frequent enough to notify the bank within the 24 hour window required for recovery of funds.
B. Incorrect. Monthly bank reconciliations are certainly not frequent enough.
C. Correct. Daily reconciliations are what's required if you are to notify the bank within 24 hours of an unauthorized transaction.
D. Incorrect. Never reconciling your bank accounts is a horrid idea on many levels including the fact that you'll never identify unauthorized transactions.

2) Why is getting remittance detail for ACH payments to the supplier so important?

A. Incorrect. There is no reference in the law regarding the supplying of remittance information.
B. Incorrect. GAAP also makes no reference of the necessity of providing remittance detail related to ACH payments.
C. Incorrect. Supplying remittance information means less not more 'where's my money calls from suppliers
D. Correct. Remittance information facilitates cash application of the funds.

Glossary

Automated Clearing House Network The Automated Clearing House (ACH) Network is the backbone for the electronic movement of money and payment-related data. It provides a safe, secure, electronic network for direct consumer, business, and government payments, and annually facilitates billions of Direct Deposit via ACH and Direct Payment via ACH transactions. The Network, which is used by all types of financial institutions, is governed by the fair and equitable NACHA Operating Rules, which guide risk management and create payment certainty for all participants.

Direct Deposit. Direct Deposit via ACH is the deposit of funds for payroll, employee expense reimbursement, government benefits, tax and other refunds, and annuities and interest payments. It includes any ACH credit payment from a business or government to a consumer.

Direct Payment. Direct Payment via ACH is the use of funds to make a payment. Individuals or organizations can make a Direct Payment via ACH as either an ACH credit or ACH debit.

Direct Payment Credit Transactions. A Direct Payment processed as an ACH credit pushes funds into an account. An example of this is when a consumer initiates a payment through his/her bank or credit union to pay a bill.

Direct Payment Debit Transactions. A Direct Payment processed as an ACH debit pulls funds from an account. An example of this is when a consumer establishes a recurring monthly payment for a mortgage or utility bill, and his/her account is debited automatically. ACH credit and ACH debit transactions process quickly. Settlement, or the transfer of funds from one financial institution to another to complete the transaction, generally takes only one business days

Settlement time for Direct Payments. Specifically, the NACHA Operating Rules require that ACH credits settle in one to two business days and ACH debits settle on the next business day.

Types of payments handled by ACH The ACH Network processes two types of transactions: Direct Deposits via ACH and Direct Payments via ACH.

Workings of ACH the ACH Network is a batch processing system in which financial institutions accumulate ACH transactions throughout the day for later batch processing. Instead of using paper to carry necessary transaction information, such as with checks, ACH Network transactions are transmitted electronically, allowing for faster processing times and cost savings.

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Course name: An ACH primer: How Savvy Companies Now Pay Their Bills
Course ID: AACMSACH

Please transfer your answers to this sheet and fax them so that you do not have to fax all the pages.

Please make sure that your answers are clearly circled.

1	A	B	C	D	
2	A	B	C	D	
3	A	B	C	D	
4	A	B	C	D	
5	A	B	C	D	
6	A	B	C	D	
7	A	B	C	D	
8	A	B	C	D	
9	A	B	C	D	
10	A	B	C	D	

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CPE Exam: An ACH Primer: How Savvy Companies Now Pay Their Bills Exam

Please select the single best answer and transfer it to the preceding sheet.

1) Who initiates and ACH debit transaction?

A. Payor initiates the transaction
B. Payee initiates the transaction
C. Bank initiates the transaction
D. Either the payor or the payee initiates the transaction

2) How should remittance information related to an ACH payment be handled?

A. It doesn't really matter; it's not an issue
B. Provide as much of the detail as possible, possibly by a separate email
C. Just let the vendor know the money's coming; they don't care about the detail
D. Don't use ACH for invoices with detailed remittance information

3) Management support of an ACH payment program is:

A. Critical
B. Not an issue
C. Irrelevant
D. Nice, but not necessary

4) Which of the following groups makes an ideal candidate for your first ACH payments?

A. Your critical vendors
B. The vendors that complain anytime something goes wrong
C. Your employees for T&E
D. New vendors

5) Which of the following is a technique used to get companies to start paying using ACH instead of paper checks?

A. Insist on shorter payment terms
B. Offer slight pricing discounts
C. Insist on greater purchasing volumes
D. Offer slight pricing increases to those who pay electronically

6) When paying through the ACH, many companies try and renegotiate which of the following items?

A. Payment terms
B. Freight terms
C. Insurance terms
D. Customization terms

7) How long do you have to notify your bank of an unauthorized ACH transaction to be assured you get all your money back?

A. 60 days
B. 30 days
C. 48 hours
D. 24 hours

8) Which of the following is a recommended tactic to help prevent ACH fraud?

A. Putting ACH blocks on all accounts
B. Handling online banking activity from whatever computer is available
C. Giving wire transfer information to anyone who calls on the phone asking for it
D. Issuing refund checks from the company's general bank account

9) Your ACH policy should include all of the following except?

A. Be detailed and written
B. Integrate stringent internal controls
C. Use ACH filters on accounts where debit activity is permitted
D. Require monthly account reconciliations

10) Why is not extinguishing POs and receivers when making an ACH payment a problem?

E. If an invoice shows up it will be paid
F. It is required by law
G. It prevents a buildup of GL entries
H. It facilitates the accrual process