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HIT Policy Committee – Interoperability and HIE Workgroup, Governance Subgroup

“Other Governance Approaches” Panelist Remarks by:

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1. Please describe your organization and the role you play in your industry.

For 40 years, NACHA – The Electronic Payments Association has served as trustee of the ACH Network, managing the development, administration and the operating rules for the financial network that universally connects all 12,000 financial institutions in the United States. NACHA’s primary responsibility is to create rules that enhance the quality, integrity and value of the ACH Network. The ACH Network moves money and information directly from one bank account to another and is best known for Direct Deposit and Direct Payment via ACH, with over 87 million transactions every day throughout the United States. The ACH Network began in the early 1970s as an innovative way to allow the U.S. Air Force to efficiently pay its personnel across the country. As well as supporting traditional uses such as payroll and bill payment, the *NACHA Operating Rules* have enabled a variety of uses of the ACH Network, including person-to-person payments, Internet transactions, business-to-business payments with accompanying information, and check conversion, among other offerings. Today, the Federal government is the ACH Network’s largest user. The U.S. Department of the Treasury saves taxpayers \$885 million each year, spending \$0.09 per ACH payment versus \$1.25 for each paper check.

NACHA brings together almost 10,000 member financial institutions of all sizes and types throughout the United States, both directly and through its Regional Payments Associations. This structure allows NACHA to be inclusive of many different types of organizations, and its processes create venues for their ideas and opinions to be heard. Venues include those to suggest new *Rules* ideas, to educate the broad industry in a variety of ways, and for industry dialogue and collaboration. Additionally, NACHA’s core competency in creating operating rules has been leveraged by other organizations when faced with the goal of bringing diverse parties together. Throughout its history, NACHA has helped a broad set of industry players vet and design concepts and requirements for: *QUEST*[®] *Operating Rules* for electronic benefits transfer (EBT); public/private partnerships for child support, SSA enrollments and death notifications, state tax payments; and interoperability for PKI models and federated identity management. NACHA also served to offer support to CAQH during its initial development phase of the CORE operating rules for health care, and now serves as standards organization for the health care EFT standard.

2. How do you ensure participants adhere to your organization’s requirements? What enforcement mechanisms do you have for organizations that are out of compliance with your requirements?

The *NACHA Operating Rules* provide the legal framework for all ACH Network transactions. All participants in the Network are required to follow the *NACHA Operating Rules*. Financial institutions enter into contractual agreements with the Network Operators, and companies enter into contractual agreements with their financial institutions, obligating their adherence to the *Rules*. These contractual agreements allow the *NACHA Operating Rules* to be enforced through the legal system. By entering into an agreement to comply with the *NACHA Operating Rules*, Network participants also become subject to Network rule enforcement mechanisms.

The National System of Fines, implemented in 1998, is the enforcement mechanism for the ACH Network to help ensure compliance with the *NACHA Operating Rules*. The National System of Fines provides a means for financial institutions to report and resolve alleged violations of the *Rules* and provides for a formal channel for the evaluation of circumstances related to possible rules violations and the imposition of fines if appropriate. It also reduces exception processing for financial institutions and maintains the reputation of the ACH Network.

Any violation of the *NACHA Operating Rules* can be submitted by financial institutions involved in the transactions. Fines can range between \$0 and \$500,000 per recurrence or imposed monthly depending on the level of the fines issued.

The ACH Rules Enforcement Panel (Panel) is the final authority regarding the imposition of fines when there is a violation of the *NACHA Operating Rules*. The Panel meets on a monthly basis to review cases and make decisions in accordance with Rules Enforcement procedures included in the *NACHA Operating Rules*. Industry volunteers who participate on the Panel include representatives from: small, medium and large asset commercial banks, credit unions, Regional Payments Associations and the ACH Operators.

3. How do you manage the evolution of policy and technology requirements (i.e. how do you adopt new standards and retire those that are no longer in use)?

Through its collaborative, self-governing model, NACHA, and the almost 10,000 member financial institutions it represents, have facilitated the expansion and diversification of electronic payments on the ACH Network over 40 years, supporting Direct Deposit and Direct Payment via ACH transactions, including ACH credit and debit transactions; recurring and one-time payments; government, consumer and business-to-business transactions; international payments; and payments plus payment-related information. With NACHA’s expertise and guidance, the ACH Network is now one of the largest, safest, and most reliable payment systems in the world, creating value and enabling innovation for all participants. Throughout the past 40 years, the ACH Network has been in a state of continuous change, adapting to changes in technology, regulations, and needs of the Network users.

Operating Rules Incorporate Standards

The *NACHA Operating Rules* encompass both operating rules and standards. It is the interweaving of the standards and the rules that has allowed for more fluid change in the ACH Network over time. Although some may refer to “operating rules” interchangeably with “standards,” there is a significant difference that manifests itself upon implementation and in the resulting benefits to the participating entities. Most often, rules define the rights, obligations and warranties of parties involved, while standards establish formatting requirements.

Operating rules establish the roles, rights and responsibilities of the parties exchanging data and/or value, and often prescribe the process to enable transaction initiation, processing and completion, error resolution, and liability apportionment. The *NACHA Operating Rules* also define data formats when specific, consistent data is required from all Network participants. By specifying the required data formats in the *Rules*, the *Rules* enforcement mechanisms can also be applied to ensure all follow the formats.

The primary purpose of standards is to establish technical requirements on the basis of a level playing field, thereby encouraging broad applicability and low barriers to entry by establishing certainty around the necessary requirements among parties to a transaction. For electronic payments, standards in combination with operating rules define data formatting and transmission requirements, so that the data is interoperable among all parties to a transaction and any technology and service providers. This interoperability has been key to successful use of the ACH Network, as all receiving financial institutions (and those who provide services on their behalf) are required to and must be ready to accept payments and related information in a consistent manner.

The *NACHA Operating Rules* incorporate the data formatting standards for all ACH transactions. This interweaving of *Rules* and standards ensures that any ACH transaction, regardless of who initiates it, can be processed in an identical manner by any other Network participant. Through the *NACHA Operating Rules*, these data formats can be altered or new ones created, to meet the needs of ACH Network users as needs change over time. Currently ASC X9 and X12, UN/EDIFACT and XML messages or data segments are carried through the ACH Network. Changes to any of these standards may not require that the *NACHA Operating Rules* or ACH formats have to change. Conversely, changes to the *Rules* or formats can be made without requiring a change to relevant standards.

In addition to the data format standards for all ACH transactions, the *NACHA Operating Rules* also incorporate standards for the formatting of payment-related information that is often carried with a transaction. For example, with respect to business-to-business payments, the NACHA payment format can accommodate remittance information in any version of the standard EDI formats. This ensures that business trading partners can exchange remittance information with each other across the ACH Network. The Federal government is a significant user of this capability of the Network.

The *NACHA Operating Rules* also accommodate a number of other “banking conventions” for formatting data using valid EDI data format standards for specific objectives. Case in point, the

NACHA Operating Rules currently support healthcare-related payments and information, and utilizing the ANSI ASC X12 835 and 820 transaction sets allows the payment and related information to flow through the Network. Several other uses support government-related purposes or mandates, such as remittance information that accompanies tax withholdings and child support payments.

In all of these examples, there are “rules” that govern the party who may initiate the payment and the responsibilities of each of the parties to the payment, and there are data formatting requirements and “standards” that enable the transactions to be processed efficiently by all parties. In order to deliver efficiencies throughout the industry, not only standards, but also operating rules that build upon those standards, are vital to an effective nationwide program and its sustainability.

Private-Sector Rules Development

Critical to the success of the *NACHA Operating Rules* is that they are amended through a deliberative and inclusive process similar to that used by Federal agencies under the *Administrative Procedures Act*. The process is inclusive, transparent, and adaptive to the needs of the electronic payment marketplace. All participants in the Network – commercial banks, community banks, credit unions, large corporations, small businesses, consumer advocates, and industry vendors – have the opportunity to comment on proposed rule changes. When needed changes are required for the benefit of the Network, there is a methodical, prescribed manner by which options are considered, impact is assessed, and voices of all participants are heard.

The rulemaking process is not brief, but it is flexible in terms of adapting to changes in the landscape, technology, and risk. Proposals for new rules may come from members of the Payments Innovation Alliance (formerly known as NACHA Councils), or from individual organizations, and they are raised up via a structured evaluation process. The Payments Innovation Alliance is a venue for dialogue around issues and opportunities where companies of all types and sizes can learn from each other.

All proposals to amend the *NACHA Operating Rules* are overseen and initially reviewed by NACHA’s Rules and Operations Committee, which is composed of a representative sample of financial institutions (by size, type, geography, etc.) as well as representatives of Regional Payments Associations, the Network Operators, the Federal Reserve Board of Governors, a corporate user, and the U.S. Department of the Treasury. The Committee determines whether a rule proposal is warranted; if so, the proposal is assigned to a rules work group (itself composed of a similar representation) for research and development. A rules work group will obtain additional input on a proposed rule from Network users, technology and service providers, and other industry representatives. When a rules work group reports back to the Committee, the Committee determines whether the proposal will be issued publicly for comment.

NACHA accepts and reviews comments on a rules proposal from any party, from any type of organization. These comments are reviewed by both the rules work group and the Rules and Operations Committee in determining whether a proposed rule should be formally adopted. If so,

the proposed rule is presented to the entire NACHA membership for balloting. The membership includes the financial institutions that are ultimately responsible for the integrity of the payment and the dollars behind it. Allowing for “request for information” and/or “request for comment” prior to a Rule ballot ensures that voices of many can be heard, and that up to date information can be considered before making a Rule. Rules ballots are issued multiple times each year, resulting in fluid changes as needed over time. Over the past 25 years, the rulemaking process has facilitated the adoption of 275 rules, creating value for users and ensuring the safety, security and convenience of ACH payments.

As rules are being developed and especially once a ballot is approved, NACHA also supports a comprehensive framework for the delivery of education to audiences across the United States, consisting of offerings it delivers at the national level, grassroots education conducted by its Regional Payment Associations, and collaborative efforts it undertakes with other strategic partners. Education is a key component of effective rulemaking, as it ensures that full implications are understood. Topics range from focused, tactical instruction to broader, strategic topics.

4. What is your organization’s business model?

NACHA is a not-for-profit association responsible for the administration and enforcement of the operating rules for the ACH Network – the *NACHA Operating Rules*. We represent and bring together almost 10,000 member financial institutions of all sizes and types throughout the United States, both directly and through our Regional Payments Associations, and hundreds of other companies and organizations of all types through our industry Payments Innovation Alliance. Our structure allows us to be inclusive of many different types of organizations, and our processes create venues for their ideas and opinions to be heard. NACHA works closely with the Federal Reserve and government regulators, member financial institutions, Regional Payment Associations and Network users to align priorities and rules. The organizations that are ultimately responsible for the payment and the funds behind it – all financial institutions – financially support the rulemaking and Network development processes. They individually and equally pay an annual fee per organization, as well as a per transaction fee to support the efforts of the NACHA organization in the areas of rule making, risk management, rules enforcement, ACH Network messaging and outreach, and Network development.

5. What lessons learned from your experience do you think would be applicable to health care?

Operating rules can drive efficiencies.

The combination of using and enforcing both operating rules and standards promotes economies of scale and consistencies of payments and related information in financial services. The same is true for the health care industry. Any transactions will need to be secure, and conform relative to syntactic and semantic definitions. Standards will help to define those areas of conformity. All

players in an ecosystem can assist in the enforcement of standards and promote adoption. The operating rules themselves will facilitate the understanding of roles and responsibilities that will most directly simplify the payment and remittance process. The rules require systemic solutions and data formatting for all participants which will facilitate the straight-through processing of all electronic transactions.

With the Federal government as a large user of the ACH Network, it was rapidly acknowledged that a national, not a regional system would provide the greatest efficiencies. The rapid evolution from regional compacts to national operating rules administered by a national entity eliminated multiple points of variations, enabled full interoperability, and drove participants to agree to common rules. Although difficult to engage all across the country, it can be done. Private sector rulemaking has allowed the financial services industry to: foster innovation, enable efficiency, ensure interoperability, and create certainty amongst participants – thereby creating value for all.

Balance and adaptability are important.

As the payments landscape has grown and evolved, so too, have the *NACHA Operating Rules*. Through four decades of administering the *Rules*, time and again, NACHA has identified the themes of balance and adaptability as elements central to the evolution of the ACH Network, the EFT standards, and the *NACHA Operating Rules*. Balance is essential in both the *Rules* themselves and the processes through which they are amended. Balancing is required to consider:

- Risk versus innovation;
- Speed of rulemaking versus broad inclusiveness;
- Cost versus benefits;
- Inclusiveness of, and impact on, all types and sizes of participants.

Operating rules allow for flexibility in balancing these trade-offs, especially the fine balance between risk and innovation where the assignment of roles, responsibilities, and recourse is essential. *Rules* have evolved over time to become aligned with regulations and technology, as changes occur. It is critical that any rule making process be flexible, timely and adaptive to the needs of the industry and not bound by arbitrary timeframes for change and enhancements.

Start early and be adaptive.

Processes need to be iterative, flexible, and adaptive over time. With technology rapidly changing – raising opportunities as well as risk – it is fair to say that we cannot accurately predict the future. If necessary, “opt-in programs” can test technology as well as impact in an effective way before an operating rule is formally adopted or changed; yet we have also learned that without “ubiquity” – without reaching all receiving institutions consistently – value is not delivered to all. *Rules* have provided us the flexibility to be adaptive of technology changes and user changes, with multiple enhancements to *Rules* each year. The inclusion of “guidelines” along with the *NACHA Operating Rules* has proven to be an excellent tool to provide further clarification to entities that need to

implement the *Rules*. The *ACH Guidelines* provide specific information about the different ACH applications including best practices, implementation instructions, and some mapping requirements.

All processes need to be inclusive, and education is required.

Participants in financial services are as diverse as those in healthcare – spread across the United States, of various sizes, sophistication, and with various organizational and business requirements. Therefore, rulemaking processes should be inclusive and raise up opportunities for many voices to be heard. Additionally, outreach via education and training is important, so that all parties fully understand their rights and responsibilities. Through work with the Regional Payment Associations, NACHA not only developed processes to hear the voice of many, but also has processes to train and educate many to foster understanding and compliance with applicable rules, regulations, and standards. Education and training also provides a venue for introduction of innovative solutions and technologies balanced with sound risk management, and an opportunity to understand, then develop, evolve, and adopt appropriate business practices. With ongoing changes in healthcare, education and outreach to all possible participants will be as important as deciding upon the change itself.