



INTERNATIONAL ACH TRANSACTIONS

ACH PAYMENT SCENARIOS: DOMESTIC OR INTERNATIONAL?

July 24, 2007

Several scenarios are provided below to better understand when a specific payment transaction involving the U.S. ACH Network would be deemed an International ACH Transaction (IAT) or a domestic ACH transaction. In all scenarios, the *location of the financial agencies involved in the processing and settlement of the transaction is the key determining factor*. Financial agencies are primarily intended to mean depository financial institutions, but also cover money transmitting businesses to the extent they are involved in the payment transaction.

While the scenarios described below represent an assessment of situations that are likely, they are not all-inclusive as to the types of transactions and situations that might give rise to a determination of an IAT or a domestic ACH transaction. Domestic transactions are listed in scenarios A, B, C/D, and part of the transactions for scenario F. IAT transactions are listed in scenarios C/D - Alternatives 1 & 2, E, G, H and part of the transactions for scenario F.

Each scenario involves defined parties as recognized in the *NACHA Operating Rules* and through proposed changes that would govern IATs under the IAT SEC code.

INTERNATIONAL ACH TRANSACTION - DEFINITION

International ACH Transaction or IAT entry means a credit or debit Entry that is part of a payment transaction¹ involving a financial agency's office that is not located in the territorial jurisdiction of the United States. For purposes of this definition, a financial agency means an entity that is authorized by applicable law to accept deposits or is in the business of issuing money orders or transferring funds. An office of a financial agency is involved in the payment transaction if it (1) holds an account that is credited or debited as part of the payment transaction; (2) receives payment directly from a Person or makes payment directly to a Person as part of the payment transaction; or (3) serves as an intermediary in the settlement of any part of the payment transaction. IAT entries must be originated using the IAT Standard Entry Class Code.

SCENARIOS

Scenario A – Payroll: A U.S.-domiciled company with 500 U.S.-resident employees is a subsidiary of an offshore multinational corporation with its headquarters in Europe. Revenues are generated through domestic business activities of the U.S.-domiciled company.

¹ See *NACHA Operating Guidelines* chapter on International ACH Transactions for further guidance on payment transaction.

Twice monthly, the U.S.-domiciled company sends payroll payment instructions for all 500 U.S. employees in a single file to its New York bank where it holds an account.

Upon receipt of the payroll information from the U.S.-domiciled company, the New York bank executes the following payment transactions:

- ◆ Originates an ACH file of 420 credit entries to pay 420 of its employees on settlement date, with an offsetting book-entry debit to the company's account at the New York bank totaling the sum value of all 420 credit entries;
- ◆ Prints and ships to the company 80 payroll checks (and 500 payroll stubs), drawn on the company's U.S. bank account at its New York bank, to pay those U.S. employees not on Direct Deposit.

Result - Domestic or IAT? All 420 ACH credits and the single, offsetting debit in this scenario would be domestic transactions and not IATs (the credits would be PPD entries; the debit typically would be an on-us DDA entry). This is because the New York bank and the RDFIs holding the employees' accounts are the only financial agencies involved in the transactions and they are all in the territorial jurisdiction of the U.S.

Scenario B - Payroll: A U.S.-domiciled company with 500 U.S.-resident employees is a subsidiary of an offshore multinational corporation (the parent company). The parent company has centralized many of the global treasury, human resources, and data processing functions of its global subsidiaries (including the U.S. subsidiary) at its headquarters in Europe.

Twice monthly, the U.S. subsidiary sends the parent company any changes to employee status, salaries, hours, etc. Also, twice monthly, after updating its central HR records, the parent company sends payroll payment instructions for all U.S. employees in a single file to its New York bank on behalf of the U.S. subsidiary which holds an account with the New York bank. Funding for payroll is generated through business activities of the U.S. subsidiary.

The New York bank receives the U.S. subsidiary's payroll file from the parent company, and executes the following:

- ◆ Originates an ACH file of 420 credit entries to pay 420 U.S. employees on settlement date, with an offsetting book-entry debit to the U.S. subsidiary's account at its New York bank totaling the sum value of all 420 credit entries;
- ◆ Prints and ships to the U.S. subsidiary 80 payroll checks (and 500 payroll stubs), drawn on the subsidiary's U.S. account at its New York bank to pay those U.S. employees not on Direct Deposit.

Result - Domestic or IAT? All 420 ACH credits and the single, offsetting debit in this scenario would be domestic transactions and not IATs (the credits would be PPD entries; the debit typically would be an on-us DDA entry). This is because the New York bank and the RDFIs holding the employees' accounts are the only banks involved in the transactions. No financial agencies located outside of the territorial jurisdiction of the U.S. are involved in the payment transactions.

Scenario C - Payroll: A U.S.-domiciled company with 500 U.S.-resident employees is a subsidiary of an offshore multinational corporation (the parent company). The parent company has centralized many of the global treasury, human resources and data processing functions of its global subsidiaries (including the U.S. subsidiary) at its headquarters in Europe. It has also centralized many of its HR-related banking functions with an international bank headquartered in Europe.

Twice monthly, the U.S. subsidiary sends any changes to employee status, salaries, hours, etc. to the parent company. Also twice monthly, after updating its central HR records, the parent company sends payroll payment instructions for all 500 U.S. employees in a file to its international bank in Europe on behalf of the U.S. subsidiary.

Upon receipt of the payroll file for the U.S. subsidiary from the parent company, the European bank instructs the bank in New York via a SWIFT message (or proprietary system) to execute the following payment transactions:

- ◆ Originate an ACH file of 420 credit entries to pay 420 U.S. employees on settlement date, with a debit to the U.S. subsidiary's account at its New York bank totaling the sum of all 420 credit entries;
- ◆ Print and ship to the U.S. subsidiary 80 payroll checks (and 500 payroll stubs), drawn on the U.S. subsidiary's account at its New York bank, to pay those U.S. employees not on Direct Deposit.

Result - Domestic or IAT? All 420 ACH credits and the offsetting book-entry debit to the U.S. subsidiary's account in this scenario would be domestic transactions and not IATs. This is because no foreign financial institution/agency was involved in the payment transaction, which started with the parent company instructing its European bank to originate a SWIFT message to the New York bank with instructions to pay the employees. The European bank is not involved in the transaction as it did not debit or credit the parent company's account as part of the payment transaction. Nor did it serve as an intermediary in the settlement of the payment transaction. Instead, the European bank was only involved in the transmission of the SWIFT payment instruction. The SWIFT message specifically instructed the New York bank to debit the U.S. subsidiary's account and not the European bank's correspondent account at the bank in New York.

Scenario C Alternative #1 (changed circumstances in italics): A U.S.-domiciled company with 500 U.S.-resident employees is a subsidiary of an offshore multinational corporation (the parent company). The parent company has centralized many of the global treasury, human resources and data processing functions of its global subsidiaries (including the U.S. subsidiary) at its headquarters in Europe. The parent company has also centralized many of its HR-related banking functions with an international bank headquartered in Europe.

Twice monthly, the U.S. subsidiary sends the parent company any changes to employee status, salaries, hours, etc. Also twice monthly, after updating its central HR records, the parent company sends payroll payment instructions for all 500 U.S. resident employees in a file to its European bank on behalf of the U.S. subsidiary. *These instructions include a request to debit the parent company's account with the European bank to fund the payroll file on behalf of its U.S.-domiciled subsidiary.*

Upon receipt of the payroll file for the U.S. subsidiary from the parent company, the European bank *debits the account of the parent company*. It then sends a SWIFT message to the New York bank with instructions to:

- ◆ *Credit its correspondent account at the New York bank on behalf of its U.S. subsidiary;*
- ◆ Originate an ACH file of 420 credit entries to pay 420 U.S. employees on settlement date, with a debit to the U.S. subsidiary payroll settlement account at the New York bank totaling the sum value of all 420 credit entries;
- ◆ Print and ship 80 payroll checks (and 500 payroll stubs), drawn on the New York bank for the U.S. subsidiary, to pay those U.S. employees not on Direct Deposit.

Result - Domestic or IAT? All 420 credit transactions would be IATs and not domestic. This is because the European bank is involved in the payment transaction by debiting the parent company's account in Europe and by serving as an intermediary in the settlement of the payment transaction as a result of funding the SWIFT message by debiting its correspondent account.

Similarly, if the payment instruction involved another funding mechanism, this scenario would result --

Scenario C - Alternative #2 (changed circumstances in italics): A U.S.-domiciled company with 500 U.S.-resident employees is a subsidiary of an offshore multinational corporation (the parent company). The parent company has centralized many of the global treasury, human resources and data processing functions of its global subsidiaries (including the U.S. subsidiary) at its headquarters in Europe. The parent company has also centralized many of its HR-related banking functions with a European bank also headquartered in Europe.

Twice monthly, the U.S. subsidiary sends the parent company any changes to employee status, salaries, hours, etc. Also twice monthly, after updating its central HR records, the parent company sends payroll payment instructions for all 500 U.S. employees in a file to their European bank on behalf of the U.S. subsidiary. The European bank maintains a correspondent banking relationship in the United States with a New York bank.

Upon receipt of the payroll file for the U.S. subsidiary from the parent company, the European bank instructs its correspondent bank in New York via a SWIFT message (or proprietary system) to execute the following:

- ◆ *Debit the European bank's correspondent account at the New York bank in the amount of the sum of all 500 payroll payments and credit an account of the U.S. subsidiary for the payroll file;*
- ◆ Originate an ACH file of 420 credit entries to pay 420 U.S. employees on settlement date, with a debit to the account of the U.S. subsidiary payroll settlement account at the New York bank totaling the sum value of all 420 credit entries;

- ◆ Print and ship to the U.S. subsidiary 80 payroll checks (and 500 payroll stubs), drawn on the New York bank for the U.S. subsidiary, to pay those U.S. employees not on Direct Deposit.

Result - Domestic or IAT? All 420 credit transactions would be IATs and not domestic. This is because the European bank is a foreign financial institution that is involved in the payment transaction in a number of ways. The European bank, which is the Originator's bank, is part of the settlement of the transaction with the New York bank by sending and funding the SWIFT message through correspondent banking.

Scenario D – Vendor Payments: A U.S.-domiciled company is a subsidiary of an offshore multinational corporation (parent company). The parent company has centralized many of the global treasury, human resources, and data processing functions of its global subsidiaries (including the U.S. subsidiary) at its headquarters in Europe.

All invoices for the U.S. subsidiary are sent to the parent company for processing and payment. Twice monthly the parent company originates a file to its European bank to pay outstanding invoices for their U.S. subsidiary. The European bank instructs a New York bank via a SWIFT message (or proprietary system) to execute payment transactions on behalf of the parties. As in Scenario C and its alternatives, the payment instructions and related funding transactions may vary.

Result - Domestic or IAT? This scenario and its various alternatives in terms of location of parties, funding and types of payment instructions are identical to Scenario C with the exception that payments are commercial in nature and not consumer. Therefore, the determination of whether the commercial ACH transactions are domestic or IATs is the same.

Scenario E -- ACH Debits for Payments to Foreign Receivers: An offshore bank provides a service allowing Persons in the U.S. to send funds easily and economically to relatives or other Persons in the offshore bank's country of domicile. The Person using the service (Originator) logs onto a website and instructs the offshore bank (Originating Bank) to make a payment to anyone in that country. The Originator keys the following information into the website: Receiver's name, physical address, banking information, and the Originator's own routing and transit number and account number of its domestic bank and physical address. The offshore bank originates a SWIFT payment instruction to its U.S. correspondent bank in New York, requesting it to originate ACH debits to its Originators in the U.S. and to credit the offshore bank's correspondent account with the amount of the debits. The instruction contains the Receiver's name, address, and other necessary information. The New York bank converts the SWIFT payment instruction into an ACH file of debit entries.

Result - Domestic or IAT? All the ACH debits originated by the New York bank on behalf of the offshore bank would be IATs and not domestic. The payment transactions involve Persons in the U.S. requesting the offshore bank to cause payment to be made to Persons in a foreign country. The offshore bank is involved in these transactions in a number of ways. First, it will ultimately credit (or instruct and fund another bank to credit) the accounts of the Receiver in the foreign country. Second, the offshore bank is involved as an intermediary in the settlement of the payment transaction, as its correspondent account at the New York bank is credited a part of the transactions.

Scenario F – Pension Payments: A U.S.-domiciled company makes pension payments to 450 U.S.-resident retirees and 50 retirees residing offshore.² Twice monthly, the U.S. domiciled company sends pension payment instructions for all 500 retirees in a single file to its U.S. bank in Kansas City, where it holds an account. Upon receipt of the pension information from the U.S. company, the Kansas City bank executes the following payment transactions:

- ◆ Originates an ACH file of 420 credit entries to pay 420 U.S. retirees on settlement date, with an offsetting book-entry debit to the company's account at the Kansas City bank for the total of the sum value of all 420 credit entries.
 - Twenty of 420 Direct Deposit payments are to retirees that reside offshore but have identified a domestic banking routing number and account number for pension payments.
 - Ten of these 20 offshore retirees hold accounts with offshore banks (in their respective host country) that, in turn, have a U.S. office in New York (the routing number in each ACH pension transaction is that of the U.S. office of the offshore bank).
 - The other 10 offshore retirees also hold accounts with offshore banks (in their respective host country) and these banks hold correspondent accounts with U.S. banks in New York (the routing number in each ACH pension transaction is that of the U.S. correspondent bank).
 - Typically, the receiving bank (U.S.-domiciled office or correspondent bank) will have instructions on file to handle the transaction – either on a book-entry transfer relationship (U.S. office) or according to a correspondent posting routine such that the proceeds can ultimately be made available to the retiree (Receiver) in his resident country.
- ◆ Prints and ships to the U.S. company 80 pension checks (and 500 pension stubs), drawn on the company's account at the Kansas City bank, to pay those U.S. and offshore retirees not on Direct Deposit.

Result - Domestic or IAT? Four hundred of the 420 ACH credits and the single, offsetting debit in this scenario would be domestic transactions and not IATs (the credits would be PPD entries; the debit typically would be an on-us DDA entry) because there are no foreign financial institutions involved in the transactions. Both the Originator's bank in Kansas City and the Receivers' banks are within the territorial jurisdiction of the U.S.

However, the 20 ACH entries to U.S. accounts for further crediting to offshore retirees would be IATs and not domestic, as they would all require an offshore bank to credit the Receivers' accounts. It is the employer's obligation to understand the legal domicile of its retirees and inquire whether they hold accounts in U.S. banks or with offshore financial institutions. The employer would have to recognize the need to provide the relevant information to the U.S. bank to facilitate origination of properly formatted IAT entries to its offshore retirees. Because the Receivers' accounts are held with offshore banks, despite being destined to U.S. bank accounts, the transactions would be IATs.

Scenario G - ACH Credit Payments to Foreign Receivers: An offshore bank provides a service allowing companies in the U.S. to send funds easily and economically to companies in its country of domicile. The offshore bank holds a correspondent account with a New York bank that can receive ACH credit entries (with remittance data), with the offshore company as ultimate

² This scenario could also apply to Social Security benefit payments to domestic and offshore residents.

Receiver. At the end of the daily processing cycle, the New York bank sends to the offshore bank (1) a wire in the amount of the aggregate of the credits received/settled that day, and (2) an EDI file with the individual entry detail and remittance information. This enables the offshore bank to reconcile the settlement wire down to the customer level and provide each customer the requisite remittance detail for their individual payments.

Result - Domestic or IAT? All of the ACH credits received by the New York bank on behalf of the offshore bank would be IATs and not domestic since the offshore bank holds accounts that would be credited as part of the transactions. Therefore, the offshore bank's offshore customers should instruct their U.S. trading partners to originate ACH entries using the IAT SEC code.

Scenario H – Money Transmitters: A U.S.-domiciled money transmitter receives a payment order from a foreign customer at one of its foreign branch offices to send funds to a Receiver in the U.S. The money transmitter makes a book entry to record the transaction on the books of its offices in both countries, and creates an ACH credit entry to send the funds to the Receiver at the Receiver's bank (also in the U.S.).

Result - Domestic or IAT? The resulting ACH credit to the Receiver in the U.S. would be an IAT and not domestic because the foreign money transmitter is a financial agency that is involved in the transaction by accepting money directly from the Originator.