Alternatives for Managing Commercial Payments Risk

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NACHA and the ACH Network

- As administrator of the ACH Network, NACHA:
  - creates and maintains the *NACHA Operating Rules*,
  - enforces the *Rules*,
  - proactively develops Network risk policy, and
  - responds to Network risk events

- NACHA implements its risk strategy by:
  - making changes to the *NACHA Operating Rules*,
  - disseminating best practices,
  - identifying industry offerings available to mitigate risk, and
  - developing tools to manage the risk profile of the Network on an ongoing basis

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Background

- Types of ACH Applications:
  - Debit transactions
  - Credit transactions
- Return codes are tracked, such as:
  - Unauthorized
  - Invalid account
  - Not sufficient funds
- "Traditional fraud" typically involved debit payments: including telemarketing fraud, credit repair, and membership clubs using ACH debit applications
  - Unauthorized debit return rates as key indicator
- Since 2001, debit unauthorized return rates fell move than 50% from .09% to .04%
- Recently fraud activity targeting businesses has resulted in fraudulent credit payments
  - ACH credits
  - wire transfers

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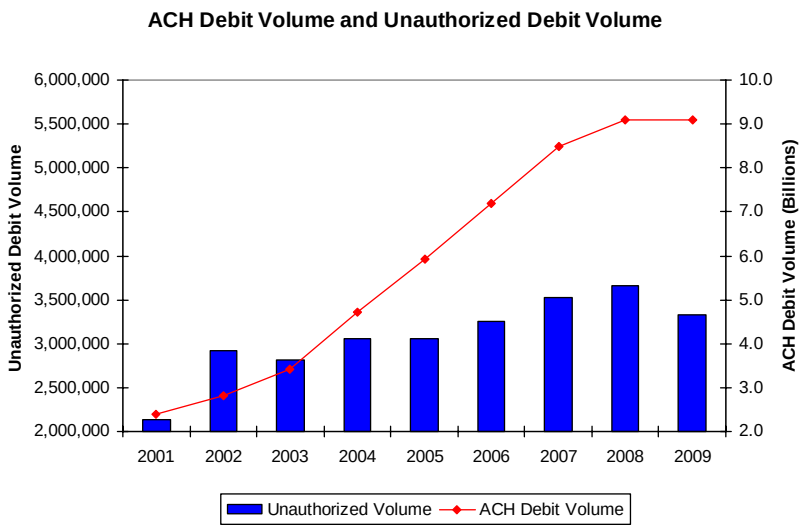
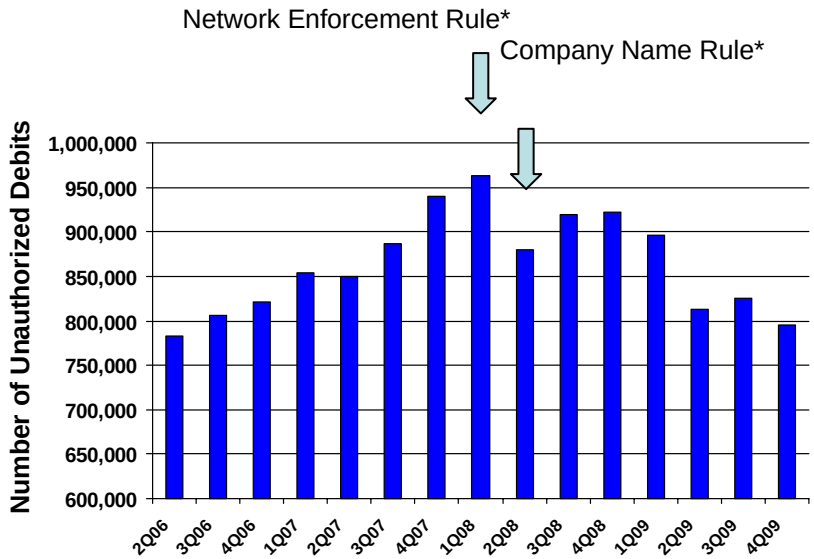
Risk Mitigation Efforts have been Robust

- ACH Debit Transactions grew 18.1% CAGR, while unauthorized returned debits grew at 5.9% CAGR
- The impact of solid Network-wide *Rules* and risk management efforts shows in the downward trend of the absolute volume of unauthorized debit returns





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What is Corporate Account Takeover?

- A type of identity theft in which cyber-thieves gain control of a business' bank account by stealing the business' valid online banking credentials through malware (among other methods)
  - Corporate account takeover is about compromised identity credentials – it is not about compromises of the wire system or ACH Network
- A computer can become infected with malware which can then spread across the business' entire internal network. This can happen through:
  - infected documents attached to an e-mail
  - a link contained within an e-mail that connects to an infected web site
  - visiting legitimate web sites - especially social networking sites - and clicking on the documents, videos or photos posted there
  - a USB port using a flash drive (that was infected by another computer)
- The cyber-thieves can then initiate funds transfers, by ACH or wire transfer, to the bank accounts of associates within the U.S. ("Money Mules") or directly overseas (with wires)

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FI and Business Partnership to Protect Against Cyber-thieves

- Smaller FIs and small and medium-sized businesses are being targeted because they are perceived by criminals as more likely to have insufficient controls
- The perception is that many small businesses do not practice dual control, do not utilize value-added banking services, and do not monitor and reconcile their accounts on a frequent or daily basis
- Financial institution and business customers have distinct responsibilities to help address the security of online access to accounts

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Recommendations for Originating FIs

- Deploy multi-factor and multi-channel authentication
- Require dual control
- Enable out of band transaction verification
- Provide out of band alerts for unusual activity
- Establish and monitor exposure limits that are related to the customers' activities
- Explore tools offered by vendors to prevent or detect fraud
- Consider the risk management services offered by the ACH Operators
  - e.g., ACH Origination Threshold/Cap
- Educating business customers is essential to risk mitigation strategies

Recommendations for Receiving FIs: How to Spot a Money Mule

- According to the FDIC, money mule activity is essentially electronic money laundering addressed by the Bank Secrecy Act and AML regulations
- How to Spot a Money Mule
  - A financial institution can look for a pattern of activity that is consistent with corporate account takeover:
    - A new account opened by a customer with a small deposit, followed shortly by one or more large deposits by ACH credit or wire transfer
    - An existing account with a sudden increase in the number and dollar amounts of deposits by ACH credit or wire transfer
    - A new or existing accountholder that withdraws a large amount of cash shortly after a large deposit (often 5-10% less than the deposit)
- In many cases, the dollar amounts of deposits and withdrawals are around $9000

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Recommendations for Businesses

- Initiate ACH and wire transfer payments under dual control. For example:
  - One person authorizes the creation of the payment file
  - A second person authorizes the release of the file
- Restrict functions for computer workstations and laptops that are used for online banking and payments
  - For example, a workstation used for online banking should not be used for general Web browsing and social networking
  - A better solution: use a dedicated computer to conduct online banking and payments activity
- Monitor and reconcile accounts daily

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Recommendations for Businesses

- Install commercial anti-virus and desktop firewall software on all computer systems
- Ensure anti-virus and security software is up to date
- Utilize routine and “red-flag” reporting for transaction activity
- Never access bank accounts at Internet cafes, or from public wi-fi hotspots (airports, etc)
- Additional resources for businesses:
  - BBB outreach to small businesses: Data Security Made Simple

NACHA Communications and Collaboration

- Partnerships are the solution to combating fraud
  - All parties have a role
  - Communicate broadly and accurately
- NACHA communications
  - 2007 and again in 2009: NACHA Risk Alerts and Members' Memos about keylogging and "Corporate Account Takeover"
  - Referenced 2005 FFIEC Guidance – Authentication in an Internet Banking Environment
- Collaboration with FS-ISAC and FBI on FI Alert
  - Communicated issues and best practices to financial Institutions and industry
- Drafted new section for Better Business Bureau Data Security publication for small businesses – "Data Security Made Simple"
- Held Teleseminars on risk / keylogging issues to educate FIs and Network participants
  - NACHA sponsored / ABA sponsored
- Risk Management Vendor Showcase – FFIEC Regulatory Panel
- Cyber Attack Against Payment Processes – in cooperation with FS-ISAC
  - February 2010 – 3 day simulation of cyber attacks
  - Raise awareness / make recommendations

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