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THE EXPANDING ROLE OF ACH IN THE ERA OF FASTER PAYMENTS

A Mercator Advisory Group White Paper Sponsored by Nacha



March 2020

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The American Economy Runs on ACH

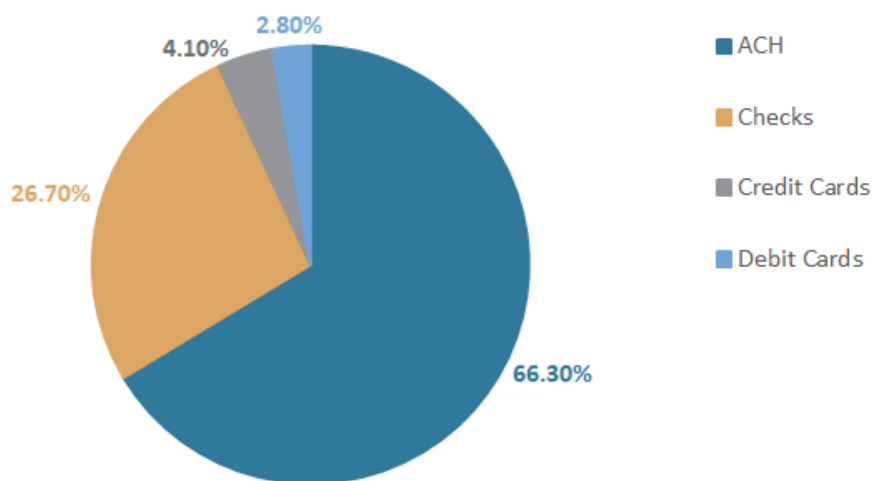
When you receive your payroll on payday through direct deposit, you likely don't give it a second thought. You know with certainty that the deposit transaction will be in your account on the assigned day. When a mortgage or car insurance payment is due, it is likely to be automatic too, accomplished through a direct debit and providing you the peace of mind that these critical bills have been paid on time, every time. These and other types of ACH transactions are the consistent, ubiquitous payments that are woven into nearly all U.S. payment form factors and use cases. ACH is the engrained payment solution that sits in the background as a reliable function that doesn't attract much fanfare and yet is critical to how we run our businesses, pay our bills, and receive government benefits and wages.

ACH is a product in its own right and is also the money movement infrastructure for other payment products. Consider that checks, online and mobile bill payments, merchant deposits, and more recently, person-to-person (P2P) apps rely at least to some degree on ACH to facilitate a transfer of funds. As we will discuss in this paper, not only is ACH continuing to grow in an established and mature market, but it is also playing an important role in emerging payment types.

Recent data from Nacha, the organization that manages the development and governance of the ACH Network, and details from the most recent Federal Reserve Payments Study illustrate the criticality of ACH to the U.S. economy. When comparing annual transaction volumes processed, ACH surpasses check volumes in the U.S. It is the stalwart of large business transactions.

Comparison of Primary Payment Types in the U.S.

Payment Dollar Volumes as a Percent of Total Volume
(2018)



Sources: Nacha and The 2019 Federal Reserve Payments Study: Initial Data Release

ACH Excels in a Diversity of Use Cases for Large and Small Transactions

The applicability of ACH to payments for consumers, small businesses, and large corporates fuels the staying power of ACH. The high ownership rate of bank accounts in the United States (currently 93%)ⁱ allows for the broad reach. Following is an overview of the importance and saturation of ACH in certain market channels and also where opportunity lies to replace non-electronic forms of payment.

Business-to-Business Channels

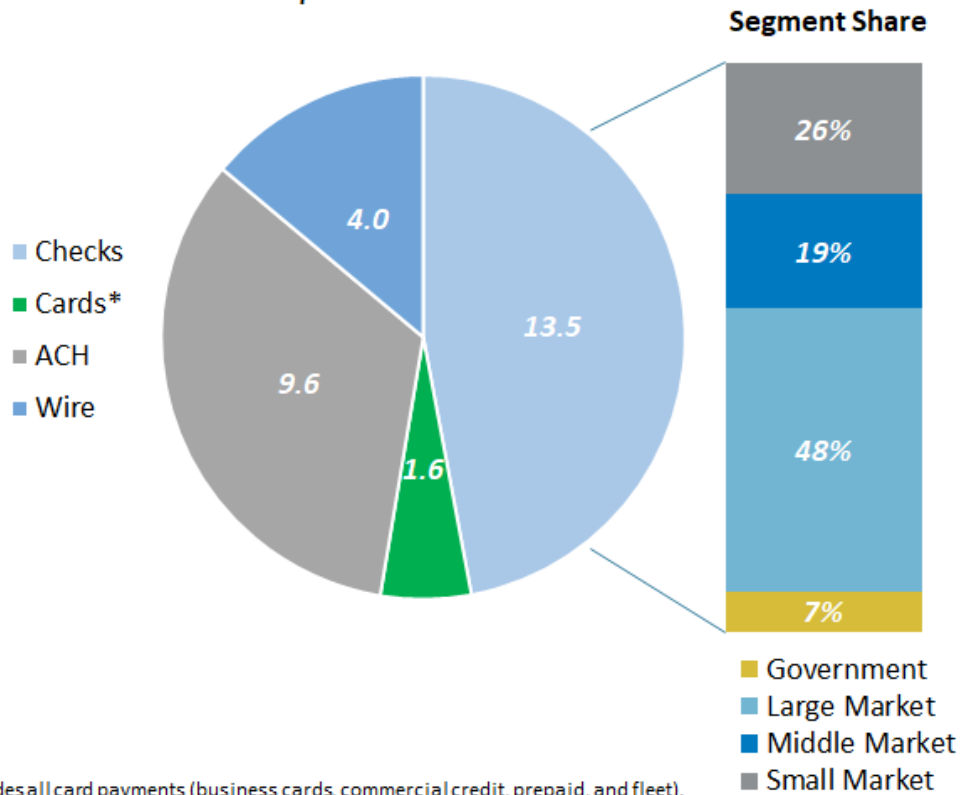
Use of ACH by businesses to pay other businesses continues to expand. Nacha reports that the number of B2B transactions grew a robust 12% and \$3 trillion in value from 2018 to 2019. The 2019 AFP Electronic Payments Summary Reportⁱⁱ found that organizations' major business customers are now more likely to use ACH than checks for payments, an important milestone. ACH is replacing check transactions for businesses for several reasons:

- Relative to the cost to other payment types, ACH represents a better value than checks. Businesses are realizing that the cost of sending and receiving checks is not just the fees their bank may charge to process a check, but the internal, often manual activities required to manage checks.
- Although no payment method is immune to fraud, businesses acknowledge that the cost of check fraud also makes checks a less desirable and less efficient payment. Seventy percent of participants in the survey presented in the 2019 AFP Fraud and Control Survey Report reported experiencing at least some fraud activity on checks compared with 33% on ACH debits and 20% on ACH credits.
- Businesses are adopting more enterprise resource planning (ERP) and accounting software solutions that automate, manage, and reconcile inbound and outbound ACH transactions.

Checks still have a presence in B2B payment activities, representing an opportunity to convert an additional \$200 billion annually in check volume to electronic payment types and inject greater efficiencies, as illustrated below.

Shifting commercial payment flows in North America provide substantial addressable opportunity to capture check transactions.

North American Commercial Expenditure, 2018
\$28.7 Trillion



Sources: Visa CCE, RPMG Research, Mercator Advisory Group estimates

Government Channels

Like corporate entities, government agencies, particularly at the federal and state levels, are very aware of the opportunities offered by replacing use of checks with less costly and more efficient electronic transactions. The Bureau of Fiscal Services has stated that most federal payments are made through ACH with few exceptions.ⁱⁱⁱ Federal benefits from agencies ranging from the Veterans Administration to the U.S. Social Security Administration are required by law to be sent through the ACH Network.

State governments are similarly focused on replacing less efficient payments. A study of the outgoing payments in the State of New York found that 52% of the transactions use checks. Converting them to electronic transactions could provide millions in savings on an annualized basis.^{iv}

Business-to-Consumer Payroll Direct Deposit

American Payroll Association found in a survey of over 37,000 consumers conducted in 2019 that 93% of the

survey participants were paid by ACH direct deposit. This percentage matches the ratio of U.S. consumers who own a checking account at a bank or credit union. When the survey respondents were asked if their paycheck was delivered on time, the very same percentage, 93%, stated that it was delivered on time, every time.^v That correlation of percentages suggests that nearly 100% of consumers who are receiving payroll through ACH are receiving it as expected on payday.

The consistency of delivery of payroll on payday means that workers are better able to pay bills and other obligations and avoid fees and late fines. Same Day ACH, the recently launched faster version of ACH, is also helping employers make sure that last minute payroll adjustments, first and last pays, and corrections are made in a timely manner as well. Direct deposit transactions are one of the fastest growth areas for Same Day ACH.

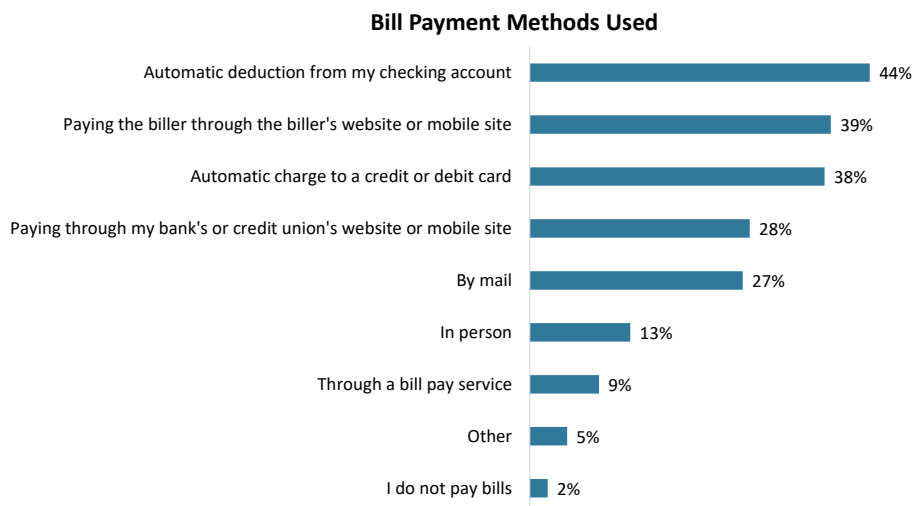
Consumer-to-Business Bill Pay

Consumers like to use a wide variety of payment types to pay bills. A study conducted by Mercator Advisory Group found that of all the payment choices U.S. consumers had available to them to pay bills, an ACH direct debit to an account is used the most often as shown in the figure on the next page.

In addition to the direct debits, consumers schedule recurring bill payments directly with their billers or through a bank bill-pay solution. These are often also facilitated through ACH transactions behind the scenes.

Consumers and businesses are flocking to subscription-based payments for everything from software licenses to streaming media to the delivery of pet treats. Businesses offering subscriptions often provide an ACH option to provide choice, to take advantage of transaction cost efficiencies, and also to avoid interruption of payments and hence service since users are less likely to have a change in the credentials of their checking account, the source of the subscription payments, unlike other payment types, which may change, requiring follow-up and sometimes a disruption of service.

Bill pay through ACH dominates other payment types.



Source: Mercator Advisory Group, North American PaymentsInsights series, 2019 Banking and Channels Survey, U.S.

Several Key Attributes of ACH Position It for the Next Generation of Payment Form Factors

ACH is entrenched in day-to-day transaction activity and is also playing a pivotal role in newer form factors, many of which are mobile-based. ACH exhibits some key features, both long-standing and newly developed, securing its relevance as new payment types emerge.

Ubiquity or the Network Effect

ACH can reach nearly every consumer, small business, and corporate account and offers the flexibility to perform both a debit and credit transaction. Consumers who have payroll cards or general purpose reloadable cards can also receive ACH transactions, reaching an ever larger audience in total. To put this into perspective, this is greater than the number of individuals with credit cards and offers the reach that other newer networks hope to achieve but are still building.

The ability to reach nearly every individual makes ACH the solution for a variety of newer payment form factors that are currently experiencing rapid growth, including some person-to-person (P2P) payment apps like Venmo and Square's Cash App as well as merchant loyalty payment apps offered by general retailers, quick service restaurants (QSRs), and convenience stores.

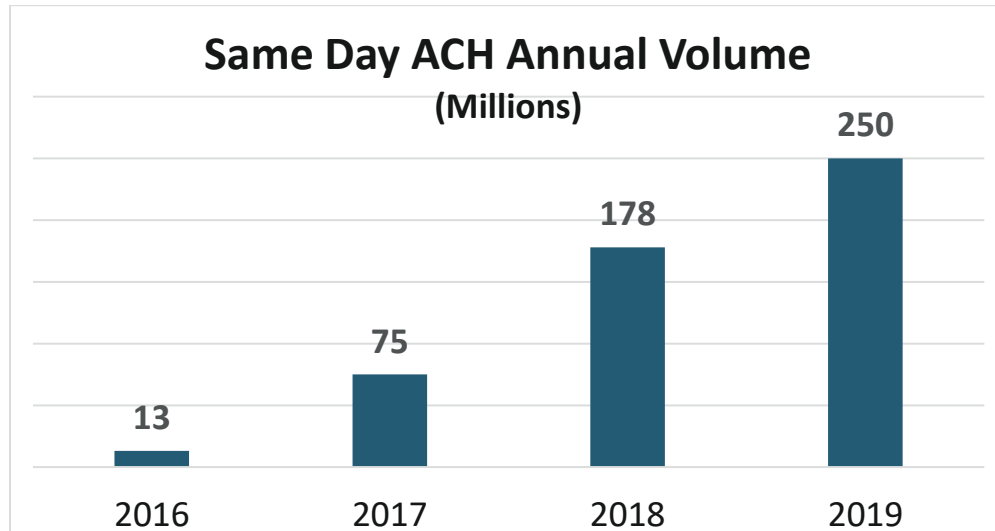
Transaction Speed Through Same Day ACH

Various faster and instant payments are launching and building volume in the U.S. Same Day ACH is one of the solutions in the continuum of faster payments when transaction speed is important. Although Same Day ACH does not meet all the criteria for an instant payment as outlined by the Federal Reserve's Faster Payments Task Force,^{vi} Same Day ACH has advantages and will have a profound impact on the adoption of other fast and instant payment solutions:

- Same Day ACH has a first-to-market advantage over other fast payments in the U.S., having been available for both credits and debits since 2017.
- Integrating Same Day ACH for both financial institutions and their clients doesn't require an overhaul of operations or revamping of accounting solutions since the transaction network and format have not been altered to offer faster delivery.
- The regulatory framework for Same Day ACH is the same as the framework for standard ACH, and so no new requirements are required or anticipated to handle exceptions like disputed transactions.
- ACH offers both credit and debit transactions that provide a level of flexibility and convenience. For example, it may be more convenient for an individual to provide approval for recurring ACH transactions to ensure that debits will be made to the person's account to cover mortgage or rent payments, insurance, or other critical transactions.
- The recently increased Same Day ACH per-transaction limit to \$100,000 will serve a broader set of transaction types. This includes use cases such as insurance claims payouts, account-to-account transfers, merchant deposit funding, and payroll funding.

Recent growth of Same Day ACH is confirmation of the value of this faster transaction. The figure below tracks the recent rise of Same Day ACH activity in the U.S.

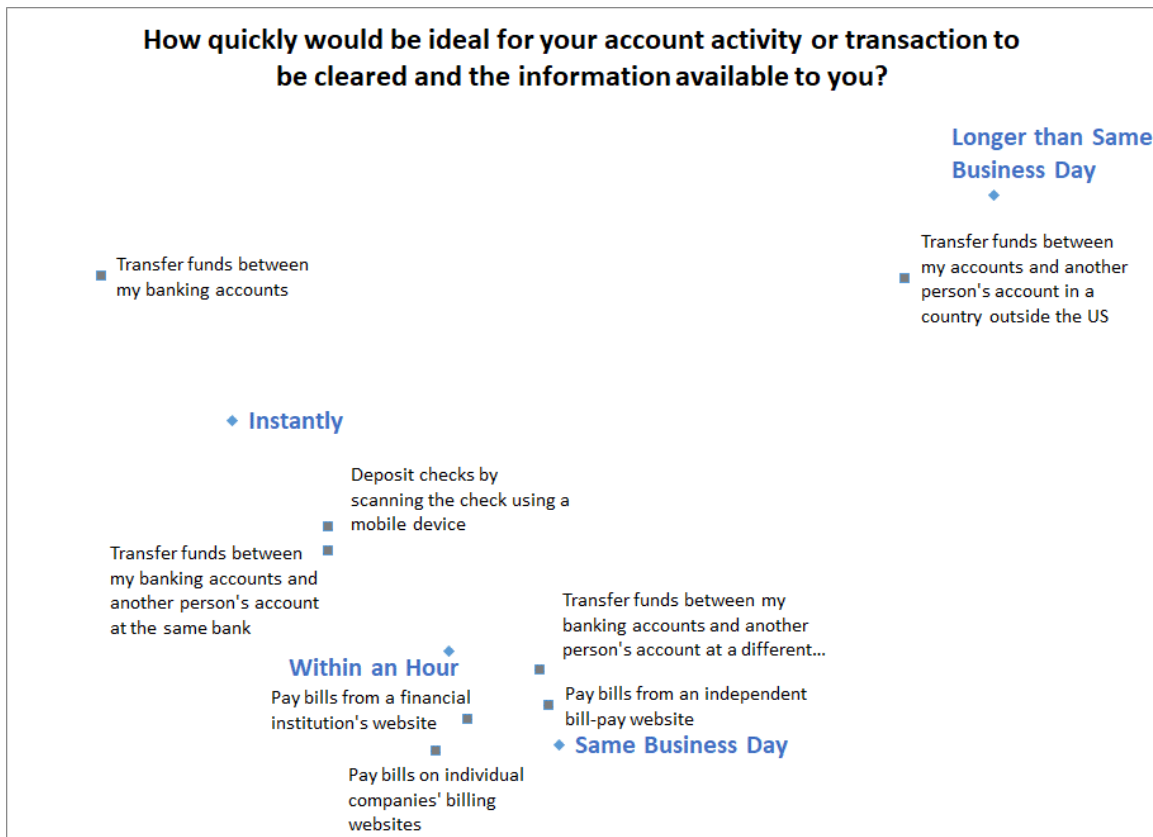
The rapid growth of Same Day ACH cements its position among faster payments.



Source: Nacha

In a recent survey, Mercator Advisory Group was interested in understanding U.S. consumers' expectations for the speed of certain transaction types. When participants were asked what would be the *ideal* timing of certain critical payments like bill payments through their financial institution or directly with a biller, or for account-to-account (A2A) transfers, many of the responses grouped in the space between "within an hour" and "same business day" as illustrated in the schematic below. This ideal scenario fits well with the delivery of Same Day ACH transactions.

Consumer expectations for payment transaction speed is within hours.



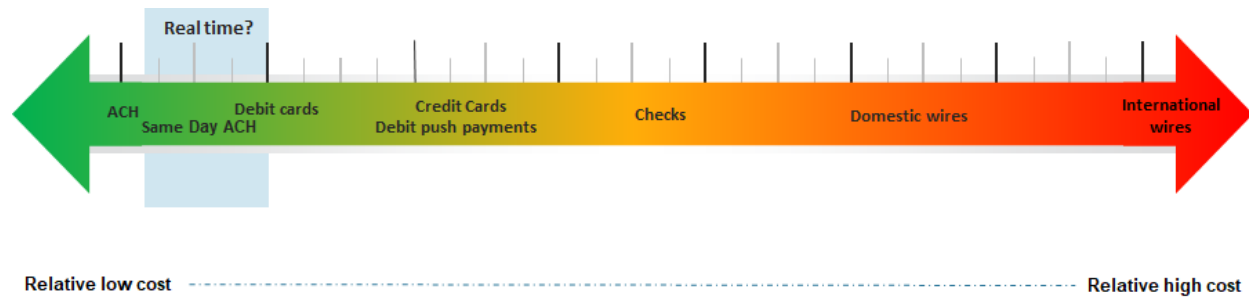
Source: Mercator Advisory Group, North American PaymentsInsights Survey series, 2019 Banking and Channels Survey, U.S.

Efficiency

ACH processes are cost-efficient compared to other payment types. The ecosystem including financial institutions, processors, and businesses, have developed systems over the decades to settle and report ACH quickly and with accuracy. When exceptions do occur, recovery is a known process. When considered in the context of other payment options, ACH is often one of the least expensive, making it accessible to more users and an option for more emerging and developing payment types. The graphic below shows the placement of payment types relative to each other based on price to end user. While instant payments are still in development and market pricing is still in flux, it is anticipated that its cost will be similar to or slightly greater than the cost of Same Day ACH. Financial institutions will determine the relative transaction costs of these solutions to their clients based on their strategies for faster payments.

Efficiency is also measured by the ease of reconciliation and hands-off processing that occurs when a transaction is received. Because ACH is a well-known and understood format, accounting and other transaction processing systems have been built around ACH to reduce the amount of intervention required to recognize an ACH payment.

ACH and Same Day ACH are cost-efficient solutions relative to other common payment types.



Source: Mercator Advisory Group

Nacha Governance

A part of the strength of the ACH Network is its unique approach to governance, which permits an open, collaborative approach to rulemaking that sets the standards for all member organizations and prioritizes and coordinates the development and launch of enhancements and new products. The membership is led by a board of directors that represents financial institutions of all sizes and with diverse business models. This private sector approach to leadership not only takes on the tasks relating to rulemaking but also provides education and certifications and acts as a leading voice for advocacy of the ACH Network in the marketplace.

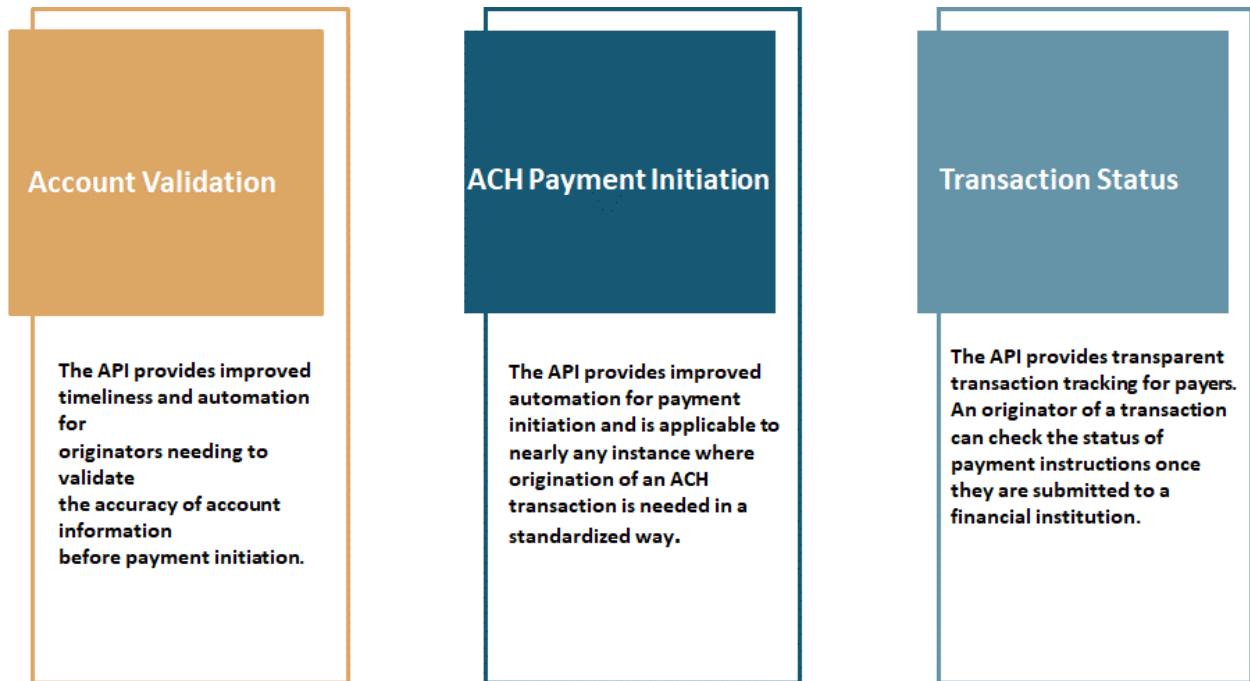
Congressional hearings in the U.S. House Committee on Financial Services were held recently regarding the emergence of instant payments platforms through both the private and the public sectors. Questions were raised by legislators regarding how these new platforms with critical importance to the U.S. payments industry would be managed and governed. Witnesses testifying at the hearing pointed to Nacha’s approach as a positive example of payment network governance that should be emulated.^{vii}

Never Standing Still

The story of ACH is ever evolving to keep pace with current payment trends, or where it’s important, to jump ahead and lead the way. New features are being launched, and some are in development or will be considered by Nacha’s membership. As an example, Nacha is taking a leadership role to standardize payment data, working across industry organizations including banks, processors, and fintechs through Nacha’s Afinis Interoperability Standards, a membership organization that works to advance API standardization and other financial services standards. This assures that transaction messaging standards are open and easily integrated with the objectives of improving efficiencies and supportive of the development and adoption of new solutions. Afinis has launched several application programming interfaces (APIs) and supports a developer sandbox and a forum for collaboration. It’s important to note that wherever possible, the ISO message standard 20022 is used since it is quickly becoming a global standard for payments including wires and instant payments.

Afinis has already launched APIs for account validation, ACH payment initiation, and transaction status, among others. Examples of how these particular APIs are being used are illustrated in the next figure.

Examples of standardized APIs and potential use cases.



Source: Nacha

Nacha’s investment and launch of Phixius is another example of how Nacha is leveraging its core competencies as a governance body, a standards organization, and an industry collaborator.

Launched in 2020, Phixius is a platform for data exchange that establishes trust between transacting parties to exchange payment-related information regardless of the payment network used. This is an improvement over the more typical environment employed today, which relies on bilateral agreements between parties that are difficult to scale. Phixius is open to all credentialed service providers like banks, networks, and fintechs, and it operates through standard rules and data formats that can create interoperability between networks, a topic of high importance in the emerging faster payments market.

To illustrate the power of Phixius, consider the use case of a small business interested in reducing its reliance on checks in its account payables operations. Through access to Phixius services offered by its financial institution, the small business can validate up-to-date account credentials of a payee, secure tax form W-9 information as well as other critical details to effect a payment that may be executed through ACH, a wire, or another payment network. This eliminates the need to join multiple directories, helps to eliminate manual processes, and minimizes errors. The small business can also create an advantage by allowing its own data to be available on the platform supporting more incoming electronic payments. The Phixius platform assures that data is up to date, users are authenticated, messages are standardized, and the platform is secure.

Supporting the Future of Payments, ACH Moves to an “Always On” Mode

Nearly \$56 trillion in transaction value and 24.7 billion transactions were processed through the ACH Network in 2019. Volume has been growing rapidly as ACH plays a prominent role in all payment channels. While ACH is an established payment type, it continues to achieve new growth goals driven by the continuous improvement that the membership champions and adoption of new solutions to meet the changing needs of the digital era. New operating expectations bring a growing need to increase availability and move to a mode that supports transactions at all hours, every day. As the ACH Network reaches for this new milestone, it will continue to support existing users and use cases as the consistently reliable and ubiquitous electric payment type.

- ⁱ <https://chicago.suntimes.com/2018/10/23/18424361/more-americans-have-a-bank-account-fdic-says>
- ⁱⁱ <https://www.afponline.org/publications-data-tools/reports/survey-research-economic-data/Details/epayments-survey>
- ⁱⁱⁱ <https://fiscal.treasury.gov/reference-guidance/green-book/>
- ^{iv} https://www.nasact.org/Files/2019_NY_study.pdf
- ^v <https://www.nationalpayrollweek.com/npw-survey/>
- ^{vi} <https://fedpaymentsimprovement.org/wp-content/uploads/fptf-payment-criteria.pdf>
- ^{vii} [U.S. Committee on Financial Services - Task Force on Financial Technology Hearing On “The Future of Real-Time Payments”](#)



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About Nacha



Nacha is a nonprofit organization that convenes hundreds of diverse organizations to enhance and enable ACH payments and financial data exchange within the U.S. and across geographies. Through the development of rules, standards, governance, education, advocacy, and in support of innovation, Nacha's efforts benefit all stakeholders. Nacha is the steward of the ACH Network, a payment system that universally connects all U.S. bank accounts and facilitates the movement of money and information. In 2019, 24.7 billion payments and nearly \$56 trillion in value moved across the ACH Network. Nacha also leads groups focused on API standardization and B2B payment enablement. Visit nacha.org for more information.