Moving to E-payments, Part Two: Are Electronic Collections Right for Your Business?

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"Despite ambitions to make a notable shift to e-payments between 2006 and 2008, corporations made only an incremental shift from 39 percent to 41 percent of total transactions, which was significantly below the goal of 55 percent set in 2006. The overall conclusion is that corporations are not overly concerned about their payment practices."

— Metavante Payment Progress Index 2008

In a previous article, "Gain 21st Century Efficiencies: Make the Move to E-payments," we explored the phenomenon of e-payment inertia and introduced a set of best practices to guide companies in the move from paper check disbursements to electronic alternatives, such as Automated Clearing House (ACH) and credit card payments. In this article, we continue the discussion with a focus on opportunities to improve the collection side of the process — by embracing electronic payment options, as well as using imaging and automation to gain efficiencies in lockbox operations.

As we explained in Part One, every corporation must evaluate whether transitioning to collecting e-payments is right for its business. Our goal is to call attention to the strategic benefits of electronic collections and demystify the process of moving to this model, so that corporations can maximize their investment in an e-collections approach.

THE HIGH COST OF COLLECTING CHECKS

If your company collects payments primarily by check, you are leaving significant cost savings on the table. Today's electronic alternatives are almost always less expensive.

Companies that collect a high volume of paper checks need one or more lockbox locations to capture and process check payments. While improvements in mail times, processing times and clearing have improved the availability of these funds, the uncertainty of these flows remains a challenge. Moreover, processing the remittance information from each check is a costly and time-consuming process, even with the advantages of lockbox technology such as imaging and data capture.

An e-payment approach to collections avoids these excess costs and delivers added benefits to the organization: It improves transparency, ensures compliance and aggregates financial data, while lessening the administrative burden of accepting paper checks. With the wide variety of electronic payment formats now available, every company should be able to find an e-payment solution that meets its needs.

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HOW TO OVERCOME E-PAYMENT INERTIA

If the reasons for moving to e-payments are so compelling, why do companies resist the change? Some worry about tracking remittance information — a valid but by no means insurmountable challenge. Others cite the float value for paper checks, which is becoming less of a factor since the Check 21 Act began allowing the majority of checks to be cleared electronically by image or conversion to ACH. The Federal Reserve predicts that within two years, it will reduce the number of check processing sites in the U.S. from 48 to 2, and virtually all items will be "local."

Lack of internal resources poses a more significant obstacle to e-payment adoption for many companies. Most treasury departments and related service areas like Accounts Receivable are significantly understaffed, and projects for these areas may not get priority for additional corporate resources such as IT support — even if they can demonstrate a return on the investment. A strategic approach that considers all of the benefits of an automated payment process can help treasury departments make the case to executive management.

SIX REASONS TO CONVERT TO ELECTRONIC COLLECTIONS

1. Save money
2. Accelerate collection flows
3. Reduce time spent on administration
4. Increase transparency
5. Improve compliance
6. Aggregate data

GETTING STARTED

The first step in moving toward an e-payments model for Accounts Receivable is to take an inventory of the collections you receive today and categorize them as follows:

- Checks received in-house
- Checks received in lockbox(es)
  - o Checks from companies (wholesale lockbox)
    - ▪ With attached remittance
    - ▪ Without attached remittance
  - o Checks from consumers (retail/wholetail lockbox)
    - ▪ With remittance stubs
    - ▪ Without remittance stubs
    - ▪ Bill pay check and list (one check covering multiple consumer payments)
    - ▪ Individual bill pay checks (one check for each individual consumer payment)
- Recurring charges
- Point of sale

The next step is to analyze each group to identify opportunities for improved efficiency.

CHECKS RECEIVED IN-HOUSE

If your customers are mailing checks directly to your offices or dropping them off in person, you need to instruct them to remit payment to your lockbox (assuming you have one). This step will improve collection flows by maintaining as many payments as possible within the single remittance stream and will likely provide better availability of funds by reducing mail and processing float.

If you do not have a lockbox, or simply want to improve the capture and deposit of these stranded items into the bank, the best approach is Remote Deposit Capture (RDC). Using a small desktop scanner and a simple Web application, you can scan these checks and transmit the digital images to the bank for rapid availability. Remote Deposit Capture takes advantage of the Check 21 legislation, which allows the clearing of checks as images. When you deposit items through Remote Deposit Capture rather than sending them via overnight courier to your

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lockbox for processing, you accelerate the time it takes to receive the funds. Besides reduced float and transportation costs, the organization benefits from an electronic process that's easier to track and manage.

CHECKS RECEIVED IN LOCKBOX(ES)

Checks from companies (wholesale lockbox)

In the simplest lockbox scenario, checks are captured and cleared and the remittance information is mailed or couriered back to the company for posting to the receivables system. But today's lockbox services can help companies move to electronic collections and an environmentally friendly process. First, they provide image capture services, which allow the processor to clear the checks as images, and then capture and post the remittance images online for use by Accounts Receivable. The transactions post much more quickly this way, saving the time and storage costs associated with handling paper remittance documents. Companies can choose the "green approach" by eliminating their daily remittance paper packages, opting to access images online at any time and using encrypted CD-ROMs for longer-term storage of lockbox data.

To automate the process even further, you can instruct the lockbox operator to capture remittance information and send it directly to your posting system, eliminating the

CASE STUDY

A U.S.-based competitive local exchange carrier (CLEC) providing telephone services across the U.S. to small and medium businesses and residential customers was working with a community bank that provided limited collections capabilities for the company's $100 million in revenue. In addition to processing lockbox transactions manually, the local bank had limited lockbox locations. The company turned to SVB for a lockbox solution with multiple locations to accelerate the receipt of its receivables and to reduce float time.

To automate the process, the company simply added a coupon to its remittance stubs. The coupon is read by an OCR scanner, which captures the information electronically and uploads it directly, thus eliminating the slow and error-prone step of keying in the data by hand.

To further automate check payments received without the needed remittance information ("check only" transactions), the company sends SVB a copy of its customer database, which SVB uses to look up missing information and reduce the number of manual exceptions to process. SVB matches checks with records in the customer database when a match is found, the remittance data is pulled from the database and a substitute scannable coupon is created for the payment. The data is then lifted from the coupon in the same way as if the original coupon had been returned and appended to their lockbox data file. The end result for this client is that nearly all of their receivables post automatically to their receivables system, thereby reducing the costly process of manually posting exceptions.

manual step of data entry in Accounts Receivable. The file is sent nightly via direct transmission, typically in a lockbox BAI file format, but customized formats usually can be accommodated. Payments received without the needed remittance information will be kicked out by your posting system into an exceptions report for your staff to handle the following morning. By freeing staff from the tedious work of remittance data entry, you create more time for following up on exceptions and reducing delinquencies and disputes.

Checks from consumers (retail/wholetail lockbox)
If your consumers are mailing checks to a lockbox with a paper remittance stub that you must then post to the receivables system, you can vastly accelerate the posting by designing the document to include a remittance coupon that can be read by an OCR (optical character recognition) scanner. The remittance information is automatically captured and sent as a file for direct upload. A true retail lockbox processes only scannable documents, thus eliminating the need for keying information off the remittance document manually by the lockbox operators. But a "wholetail" lockbox (blend of wholesale and retail) can process consumer payments received with or without the scannable coupon. Whatever data is needed for posting to your system would be scanned or keyed and transmitted in the same file for upload.

Another option for consumer payments sent in without the needed remittance information, commonly known as "check only" transactions, is to use a customer lookup service to obtain the needed information, which reduces the number of manual exceptions your team must process. To use this service, you send your customer invoice file to the lockbox operator. When a "check only" payment arrives, the lockbox operator checks the customer database for a match on two data points, usually the name and

address on the check. When the lockbox operator finds a match, they pull the remittance data from the database and create a scannable coupon for the payment. The payment is then processed automatically, and included in the nightly file for posting to your Accounts Receivable system.

Many consumers today are using bill pay services to make their payments. If you are receiving payments from these online bill pay systems, they can come in one of two forms: a check and a list of the consumers account numbers, or individual bill pay checks with the consumer account number on the memo line. Unfortunately, the list may or may not include the specific information you need to post the receivable to your system. Bill pay services also create a data entry challenge. Lockbox operators must retype account numbers from individual bill pay checks, creating the risk of errors that will cause these items to show up in the exceptions report.

A better alternative, if you have a large volume of customers sending you payments, is to contact the key bill pay providers directly, supply them with your account information and ask them to accumulate the payment instructions and convert them to ACH transactions. CIE and CTX are two NACHA (Electronic Payments Association) formats that are commonly used. Consumers use CIE transactions to initiate transfer of funds to a company through a bill payment service. The CTX format is used between corporate trading partners to transfer funds. The two largest providers of these services are Metavante and Fiserv/Checkfree. Each has a website with instructions on how to request ACH payments.

Once you have made the change, instead of receiving a check and list or individual bill pay checks, you will receive an ACH with an addenda record which your bank can provide to you as a report in your online account reporting service or send to you as a file in Electronic Data Interchange (EDI) format. Some bill pay providers can also send the remittance information directly to you electronically. Your bank may also be able to do custom programming and provide the information in a consolidated file with your lockbox remittance data.

RECURRING CHARGES

If you are billing a recurring charge such as a subscription or membership fee, the most effective and economical way to collect these payments is through ACH. This service automatically collects recurring payments authorized by your customers. To promote this service to your customers and increase adoption, you can emphasize the convenience factor—they'll no longer have to remember to write a check and ensure it is in by the due date. The service also will help the consumer eliminate late fees and avoid potential loss of service due to non-payment. Once the customer agrees to use the service, you simply set up a recurring ACH debit with your bank's online ACH service. The ACH can then be triggered to debit the customer's account and credit your account on the due date each month. This will allow you to automatically update the receivables and reduce your late or uncollected payments.

Alternatively, you can offer your customers the option of putting the charge each month on their credit card. The enrollment process for recurring credit card payments is similar and offers the same benefits to the customer, plus the additional benefits of allowing customers to extend the terms, and possibly receive reward points from the transactions. Your merchant services provider can help you to set up the recurring charges.

POINT OF SALE (POS)

If your business collects checks for purchases at the point of sale, the most obvious opportunity for moving to electronics

is to accept credit card payments. Numerous studies have shown that when customers are given the opportunity to pay with a credit card, they spend more than if they were to pay cash or write a check. Credit card transactions also take place more quickly than checks, allowing you to serve more customers.

If you continue to accept checks, the use of a scanner for Remote Deposit Capture (RDC) can still improve the availability of the funds and eliminate a trip to the bank. When using RDC, these checks can either be scanned at the point of sale and transmitted as an image check file, or converted to an ACH debit for consumer checks and cleared as an ACH transaction called Accounts Receivable Conversion (ARC). Alternatively, you may choose to consolidate the checks and scan and clear the consumer checks as the ACH transaction called Back Office Conversion (BOC).

CONVINCING CUSTOMERS TO PAY ELECTRONICALLY

Once your company has decided to embrace electronic collections, you need to convince your customers that the transition benefits them. The idea is to make it easier for your customers to pay you electronically instead of writing a check. Point out alternative payment methods on your Web site, and provide an easy way for customers to register. They are more likely to go along with the plan if you offer alternatives such as direct debit and credit card payments. If you send invoices to your customers, include an insert that explains the benefits of changing to electronic payments and give them easy instructions to enroll.

Many companies use their lockbox remittance coupons to promote these alternative payment methods. By putting a simple checkbox on the front of the coupon and space on

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the back of the coupon for their authorization to debit their bank account monthly or charge their credit card regularly. As these remittance coupons come in, scanning devices detect the mark in the checkbox on the front and sort them out to return to the company for further processing. Some financial institutions will take it a step further and generate a file of the ACH debit authorizations that can be uploaded into their ACH system to process these recurring transactions. For credit card charges, financial institutions may either process the transactions for you or send a file that can be uploaded into your point-of-sale (POS) device for authorizations and settlement. Processing through your Merchant Services provider ensures comprehensive reporting for all credit card transactions processed, regardless of origination (lockbox coupon, POS, website, etc).

If you are sending invoices or bills in the mail, consider moving to electronic delivery and providing a mechanism within the receipt of the invoice or bill for the customer to provide a payment instruction of either a debit to their account through ACH or a credit card number.

NEXT STEPS

As mentioned at the outset, the case for converting to collecting e-payments often makes sense to corporate leaders. Yet there is considerable inertia to overcome in order to get a commitment to implement. It may require a coordinated campaign on the part of your treasury department to bring your collections process into the 21ˢᵗ century. In our experience, there are three key elements to a successful campaign.

1. **Cost/benefit analysis.** The cost of receiving checks and paper remittances and the data entry of the remittance information to the accounts receivable system should be factored against the costs of automating your in-house or lockbox capture. The analysis of accepting credit cards and the inherent interchange fees should be offset by the reduction of costs in posting the receivables. Be thorough and objective in your analysis. And remember, ROI isn't the real story; it's the strategic benefits, which you need to describe in a separate report.

2. **Strategic benefits report.** Up-front monetary savings are just the beginning for companies transitioning to collecting e-payments. Once implemented, companies reliably experience reduced administration, greater transparency of cash flows, an improved ability to document compliance and the many proven business benefits that come with data aggregation. The time it takes to resolve payment inquiries with your customers will come down significantly by moving to electronic payments, freeing staff to focus on more strategic activities. Be sure to discuss all of these topics as they apply specifically to your organization.

3. **Best practices and vendor selection.** Obviously, there are issues of security, reliability and efficiency in implementing an e-payment system. One of the best sources for information on best practices in implementing electronic payment solutions will likely be your local or national treasury management professional organization. In the U.S., the largest such organization on the national level is the Association for Financial Professionals, available online at www.afponline.org

Your treasury department's case will be compelling because you will have performed the due diligence needed to make a successful transition to receiving e-payments.

If you require guidance in preparing your case, or creating a plan for implementing e-payments in your organization, it makes sense to contact your Treasury Management Sales Officer or Product Advisor.

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