

In the current uncertain economic conditions, treasuries want quicker availability on incoming payments and are optimizing processes just as recent technology innovations are helping to boost availability and re-launch lockbox services.

BY RICHARD GAMBLE

Lockbox Lift-Off

Though “lockbox” is hardly mentioned in national elections anymore, the venerable wholesale lockbox is becoming a more efficient payment processing factory, and aggressive banks are building out their lockbox operations to provide more comprehensive receivables management solutions. “Our end-to-end process gets faster all the time,” boasts Doug Hartsema, managing director of J.P. Morgan Treasury Services. “And error rates keep coming down. Every year we beat our previous year’s performance. For banks that invest in the best technology, the product keeps getting better and better.” And just in time. With the current rocky economy and credit crunch, treasuries want quicker availability on incoming payments and are optimizing their processes to

get it, reports Annette Hazapis, director of collection product management at KeyBank. That has modestly boosted demand for lockbox services, she says. “Some companies that have never used wholesale lockbox are now actively considering it.”

Two relatively recent innovations are helping treasuries expedite availability. One is the technological ability and the legal authority to convert a paper check into an electronic check image and transmit the image through check-clearing channels. The other is the back-office conversion initiative that permits companies to convert consumer checks to Automated Clearing House (ACH) transactions in their own back office and then clear the payments through ACH channels. Which way is better depends on individual circumstances, Hazapis says, but both are more efficient and result in quicker availability than physically transporting paper.

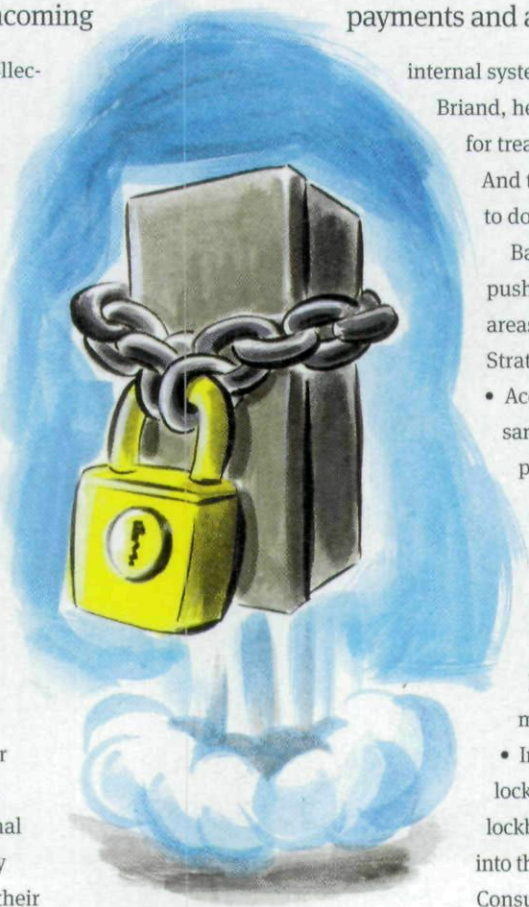
Treasuries are looking for more than optimal check clearing and quickest availability. They also want to get remittance data to flow into their

internal systems quickly and automatically, notes Al Briand, head of product management and strategy for treasury services at Bank of New York/Mellon. And they’re turning to bank lockbox operations to do this, he reports.

Banks, with treasury encouragement, are pushing the lockbox frontier forward in three areas, says Dave Robertson, partner at Treasury Strategies Inc., Chicago. They are:

- Accelerating the resolution of exceptions with same-day decisions on how they should be posted. Corporations then get clean file postings and a more accurate real-time picture of their liquidity and credit positions.
- Pursuing industry segmentation strategies that focus on the specific payment documents associated with health care, property management, government and so forth.
- Integrating remote deposit capture with the lockbox so that check payments that evade the lockbox can be imaged and remotely deposited into the lockbox work flow.

Consultant Craig Jeffery adds a fourth: Banks are



starting to take over the process of sending out invoices—getting a file from a company's A/R system and converting it to electronic invoices that are sent over the Internet and paper invoices that are mailed. If a bank sends out the invoices, it's already prepared to match them with incoming payments, notes Jeffery, managing partner of Strategic Treasurer LLC in Atlanta.

Lockbox is becoming more and more an automation and scale business. Banks that buy the best technology get higher productivity and lower costs. Banks that don't buy the technology are getting out of the business or outsourcing to the high-tech, high-volume shops, Treasury Strategies' Robertson says.

One overnight data transmission is still standard, but a few high-volume users are getting them more often, Hartsema notes. And about a quarter of JP Morgan Chase's lockbox clients are now using the alert feature for intra-day notification.

While the lockbox as an incoming check and remittance document processing factory is mature and sophisticated, there's still plenty of room for improvement in integrated global collections. The goal is a global collection strategy that not only makes cash available as soon as possible but creates straight-through processing for all payment types in all currencies from all global collection points, says Ray Fattell, senior vice president for North American product management in HSBC's global transaction banking unit.

HSBC operates both foreign and domestic lockboxes and provides file transmissions that can be consolidated for posting to a central enterprise resource planning (ERP) system or sent to a regional treasury or shared service center, whichever a company prefers.

Top banks long ago expanded their receivables processing reports to include ACH and wire transactions as well as checks, but card-based payments, a growing share of many companies' receipts, have eluded such integration. "Like many banks," says Tom McGahan, senior vice president and head of receivables product management for Wachovia Treasury Services, "we're trying to make that link."

Having a bank capture and transmit key

data from remittance documents along with payments is one old service that is capitalizing on technology improvements to streamline the process. Better image quality and intelligent character recognition (ICR) software programs gradually are displacing manual keying to capture remittance detail, Hazapis reports.

Automated data capture comes through a combination of three techniques, Robertson says. One is forms recognition. The system reads a document once and creates a template. When that vendor shows up again, identified by ABA and account number, the template is applied to automatically lift the relevant remittance information. Then there is contextual processing. The system looks for the key words like "Invoice Number" and whatever follows is lifted as the invoice number. Finally, there is roping. An operator finds the information that must be captured from the on-screen image, creates a field around it and then uses ICR to read what is in that field.

It works, but imperfectly. While many retail and government lockboxes now require little manual data capture, due to machine-readable coupons (retail) and standardized forms that can be templated (government), corporate-to-corporate wholesale is still a messy world with a lot of manual key-stroking. It's done from images on a screen instead of stacks of paper, but it's still a highly manual process. JPMC recorded 2 billion wholesale lockbox keystrokes last year, and "less than 50% of the data-capture is technology-aided," Hartsema says. (Robertson estimates 30% automated capture is closer to the industry standard.)

The technology is fallible, McGahan says, and companies have to decide how much tolerance they'll accept for uncertain capture. If they set the bar high, they'll have few errors but a lot of kick-backs. If they set the bar low, they'll have less manual processing but greater risk that some characters will be misread and insert errors in the data file.

The most productive wholesale lockbox frontier may be extending the reach of the service forward into cash application and exception management, the real pain point for many internal A/R operations. "Many companies suffer from poor handling of that critical

Companies want to get remittance data to flow into their internal systems quickly and automatically, and they're turning to bank lockbox operations to do this.

—BANK OF NEW YORK/MELLON'S BRIAND



last part of the A/R process," McGahan says. Wachovia is developing cash application and deduction management software that he calls "a slick tool."

Adding value to the traditional lockbox product means moving forward in the workflow to match incoming payments to the right receivable and even taking the first step or two to investigate and resolve payments that don't match receivables, explains Don Schule, North American head of receivables solutions for Citigroup.

"We're getting closer to our clients' ERP systems," Schule says. "We use access to their invoice and A/R systems to take the first cut at making a match. We have become, for many of our clients, the first level of resolution." For exceptions that have to be kicked back to the company for adjudication, doing that process intra-day through an interactive lockbox gets the best results.

While lockbox is still primarily a batch process business with daily transmissions, two features bring a real-time element to the service. One is the online posting of images at a bank website soon after the check and documents are processed. Someone at the collecting company can see an image of a critical payment in real-time instead of waiting for an end-of-day process. The other is an alert feature. The company can identify a time-sensitive payment and be alerted by beeper or cell phone when that payment is processed by the bank, explains Arthur Brieske, head of global payments strategy and ACH infrastructures in Deutsche Bank's global transaction banking unit.

A few leading-edge treasuries are now resolving mismatches before the transmissions occur, Robertson says. "It's complicated because it requires an inbound transmission for the bank and active management on the corporation's part, but the results are terrific," JP Morgan's Hartsema says. "They get a much higher hit rate. Banks have to learn to make it easier, but it's catching on and will become mainstream eventually," he predicts.

It works this way: a company sends the bank a file of open receivables—the payments it's expecting to get. When the bank's system gets a payment, it tries to match it

to an open receivable. Those matched payments will post automatically. "If we didn't have a receivables file, we'd just do the data entry and hope there was a match," Hartsema says. Such visibility allows a bank to resolve many mismatched payments before they get to the corporation. If a check comes in that pays seven of the eight invoices for which the company was expecting payment, for example, the bank can do a partial match so that the corporate A/R system closes out the seven receivables that were paid and leaves one open as not yet paid, he explains.

Intra-day resolution of most mismatches is still a special enhancement to lockbox processing, but it's on its way to becoming

The company can identify a time-sensitive payment and be alerted by beeper or cell phone when that payment is processed by the bank.

—DEUTSCHE BANK'S BRIESKE



standard. "It's a lot more efficient," Wachovia's McGahan insists, "than the alternative, which means physically packaging the paper around payments that don't match and shipping it to the company, which has to physically fix it on paper and ship paper back to the bank." With Online Decisioning, the mismatched payments that the bank can't resolve are flagged and posted at a bank Web site. Clients come in and review the documents and instruct the bank about how payments should be applied so that when the nightly transmission is made, a very high percentage of the transactions will post automatically, he says. If they don't get around to fixing exceptions before the cutoff, the exception will either be re-queued for consideration the next day or sent to the client as an exception to be processed manually, whichever the company chooses, he says.

Banks are pumping up their lockbox imaging and ICR technology both to craft enhanced services they can sell to corporations and to streamline their internal operations, BNY Mellon's Briand says. While many started by imaging paper only for companies that bought the imaging service, banks quickly learned that they operate more efficiently working from images on a screen, and switched to imaging everything, whether a company was paying for the service or not, he explains.

Improvements in image technology mean that paper gradually is dying at the lockbox. "We're still a huge inbound paper factory, but we're working to eliminate all paper coming out, and our sophisticated, high-volume customers no longer want paper," JP Morgan's Hartsema says. For quite a while after imaging was introduced, people held onto the paper in case there were questions and the image quality wasn't good enough to answer them. But now images are clear enough and reliable enough that treasury and A/R staffs are comfortable having the bank shred the paper, he says. "The image is now the document."

Later this year, Wachovia will introduce a "virtual lockbox" arrangement that will let companies receive and scan their own checks and remittance documents and then transmit

the images to the bank—essentially doing the first steps of the lockbox process in-house and letting the bank finish the process with data capture, transmission and image archiving. This gives them lockbox results at a reduced cost, McGahan says.

While imaging now makes checks and remittance documents very mobile, the geography isn't changing lockbox configurations much. "Accelerating the mail collection is still important, so we locate lockbox sites where we can grab the mail the fastest," Hartsema reports. Most banks aren't hiring third parties to do the mail pickup and first-pass imaging, he adds. "That's the most important part of the process. We'll hang on to that," he says. But data entry can be done anywhere, and some of it is done offshore, he says.

Wachovia is in the process of moving to a hub-and-spokes model. There will be either two or three hubs—two would be essential to provide processing redundancy—and a yet-to-be determined number of spokes where mail will be opened and documents scanned and then forwarded to a hub for further processing. Some spokes offices will be owned by the bank and some will be owned by vendor partners, McGahan says. Now that electronic images have replaced paper documents, banks can gain efficiencies from distributed processing—spreading the workload to where there is capacity to handle it.

An efficient, bank-sponsored remote deposit solution tied into the wholesale lockbox is coming. JPMC is beta-testing one, with rollout scheduled for next spring. Now checks can be deposited remotely but the remittance documents aren't incorporated into the image lockbox workflow, Hartsema reports. When that happens, it will help treasury staffs, especially around the end of reporting periods, get more payments that aren't mailed to the lockbox into the record before the reporting deadline, he explains. "It will be a more efficient way to get the stragglers in with the herd," he says.

While the volumes may not be large, the pick-up in float and control is so obvious that companies are simply doing it, without bothering to do cost-benefit analyses, Jeffery reports.

Credit Crunch Means Putting Discipline Into Collections

In a serious credit crunch, companies hoard liquidity and start paying their suppliers slower. That's what experience says. And that's what's happening, according to treasury consultant Craig Jeffery, managing partner of Strategic Treasurer LLC, Atlanta. Based on anecdotal evidence, he says that paying companies are delaying payments substantially, and the collecting companies that are hurt the most are the passive ones that don't invest in the tools and people to collect with discipline.

Statistics so far suggest it's not that bad. Actually, DSO stayed flat through June 2008, the latest numbers available, and days sales delinquent was showing a slight improvement, according to surveys taken by the Credit Research Foundation (CRF), Columbia, Md. "While the economy was booming for most of the past decade, companies kept their sales-oriented offense on the field, but now management is giving the defense real playing time, and they are tightening credit and putting discipline into collections. That is causing a slight improvement in DSD," says Terry Callahan, CRF's president.

In the face of payment stretching by customers, the wise collecting company will extend payments selectively in a negotiated, structured way and then put pressure on customers to stick to the agreement, says Hye Yu, global practice leader for customer-to-cash programs at REL, a subsidiary of the Hackett Group. "It makes for smoother, less conflict-ridden relationships," she says.

When customers break their patterns and start paying slower, it can wreak havoc on cash forecasts at a time when they are particularly critical. "You just have to watch the paying patterns carefully and give more weight to recent behavior when you adjust your forecasts," says C.J. Wimley, group vice president, order to cash solutions, at SunGard's Avantgard unit. Slower payments are partly offset by a trend for customers to pay quicker to take advantage of prompt-pay discounts, which also can throw off forecasts, he notes.

FX4Cash™

When it comes to choice and connectivity in cross currency payments, one name stands out.

FX4Cash™ delivers the best of all worlds when it comes to managing cross-currency payments. An end-to-end STP solution that combines our leading global expertise in FX and Cash Management* to bring you all the strategic choice, transparency, efficiencies and opportunities you want.

In other words, everything you need from the established No.1 because we like to make life easy.

www.db.com/fx4cash

A Passion to Perform.

Deutsche Bank



*FX4Cash is an unregistered trademark of Deutsche Bank AG. FX4Cash is part of a comprehensive range of db transaction solutions to enhance cash management efficiencies. This advertisement has been approved and/or communicated by Deutsche Bank AG London. The services described in this advertisement are provided by Deutsche Bank AG or by its subsidiaries and/or affiliates in accordance with appropriate local legislation and regulation. Deutsche Bank AG is authorised under German Banking Law (competent authority: BaFin - Federal Financial Supervising Authority) and regulated by the Financial Services Authority for the conduct of UK business. Securities and investment banking activities in the United States are performed by Deutsche Bank Securities Inc., member NYSE, NASD and SIPC, and its broker-dealer affiliates. Lending and other commercial banking activities in the United States are performed by Deutsche Bank AG, and its banking affiliates. Deutsche Bank AG Dubai branch is an authorized firm regulated by the Dubai Financial Services Authority, all services are solely directed at Professional Clients which Deutsche Bank AG Dubai branch is satisfied meet the regulatory criteria as established by the DFSA. Copyright Deutsche Bank 2008.

Copyright of Treasury & Risk is the property of Wicks Business Information and its content may not be copied or emailed to multiple sites or posted to a listserv without the copyright holder's express written permission. However, users may print, download, or email articles for individual use.