First Data

A First Data White Paper

Tipping Point for Outsourcing of Remittance Processing

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First Data Insights

Over the past 12-18 months we've seen an increasing number of businesses grappling with the issue of how to cost effectively manage their in-house remittance operations given declining paper check volumes and approaching obsolescence of their first generation image clearing systems. Investments clearly need to be made to realize the benefits of ARC and Check 21 Image Cash Letters, but will those investments pay back given that paper check volumes are forecast to fall by an additional 28 Billion by 2010?

Because so many businesses are currently developing strategies to tackle this challenge, First Data solicited the experts at Dove Consulting to draw upon the latest remittance processing research to help add dimension to the "Tipping Point" discussion. Is there a volume level at which in-house processing becomes less efficient than outsourcing? Are there trigger points, like required upgrades or increasing transport costs that impact when a company should consider outsourcing over in-house processing? We believe the answer to both questions is "yes," and have quantified the key decision points in this white paper which we hope will assist companies to define future strategies for their lockbox operations.

Introduction

In-house remittance processing has reached a 'Tipping Point' where most organizations will achieve lower cost per item through outsourcing than can be realized with in-house operations. Currently, thousands of organizations still operate in-house lockbox operations and have benefited from the innovative technology and RP system that were developed during the 1990's. However, significant changes in the payments landscape and operating economics are leading financial managers to conclude that it is better to outsource their organization's remittance processing function in order to focus their energy and capital on strategic areas in their core business where they can grow sales and margins.

Evolution of Retail Lockbox Processing

Over the past four decades, large consumer billers have operated in-house remittance processing (RP) facilities to process and deposit paper check payments that are received at their lockbox. During this period, retail lockbox processing underwent a dramatic evolution as new methods were employed to improve efficiency. Innovative use of the U.S. Postal Service led to the development of remittance mail handling that sped up mail delivery to special PO boxes set up to serve high volume billers. Enhanced delivery and presorting services reduced mail float and expedited processing of incoming mail received at lockboxes. The adoption of standardized envelopes and remittance stubs with scan lines enabled high-speed extraction, and CAR/LAR matching revolutionized bill payment processing by automating tedious manual activities. Together, these techniques allowed billers to prepare deposits with encoded checks faster, reduce float, and save money on bank fees while also efficiently posting customer payment to AR files.

As a result of these many innovations, remittance processing has become a highly sophisticated and IT-intensive operation, which is expensive to manage, staff and maintain. Furthermore, recent declines in check usage and 'disruptive' innovation in check processing are leading more billers to evaluate whether they should outsource their remittance processing to a highly specialized third-party provider, who has already invested in new systems, provides national coverage through sites distributed across the country, and can share economies of scale by aggregating volumes from multiple lockbox customers.

Check 21 Image Clearing will Reach Critical Mass in 2008

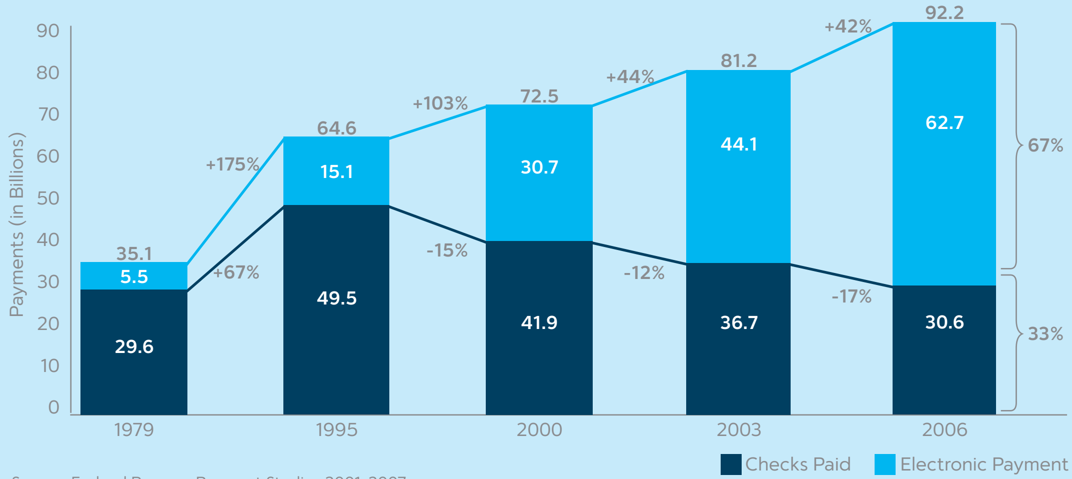
The tragic events of September 11, 2001 spurred a series of events that reshaped the RP industry. When the FAA grounded all commercial aircraft, the nation's check clearing system was temporarily paralyzed as check courier aircraft stood down. This crisis demonstrated that the United States needed a new method for presenting transit checks for clearing to ensure that consumer and business payments could be completed without the use of aircraft.

Check 21 provided the solution by granting Substitute Checks the legal equivalence of a payor's original check. The establishment of check image standards and format leveraged years of innovative work by the banking industry and its suppliers to facilitate the rapid adoption of image clearing. With the effort of the Federal Reserve and investments by check processors and clearinghouses, a national image clearing infrastructure has been constructed over the past four years. As of December 2007, ECCHO reported that over 8,603 or 52% of all U.S. financial institutions were capable of receiving check images for collection. The Fed expects 90% of U.S. banks to be on board by 2010.

Tipping Point in Paper-Based Remittance Processing

The RP industry has entered an era in which paper checks are no longer the most popular payment instrument. The Federal Reserve Bank has estimated that volume of checks paid in the United States peaked around 1995 at 49.5 billion and steadily declined to 30.6 billion in 2006.

Figure 1. Growth of Non-Cash Payments in the U.S., 1979-2006



Source: Federal Reserve Payment Studies 2001-2007

In contrast, electronic payments accounted for 67% of all non-cash payments in 2006, up from a 54% share in 2003. More importantly, between 2003 and 2006, electronic payments grew by 42%, while checks paid declined by 17%. For remittance processors, this trend of paper checks displacement by electronic payments will require profound transformation of their operations and economics.

Changing Bill Payment and Remittance Processing Landscape

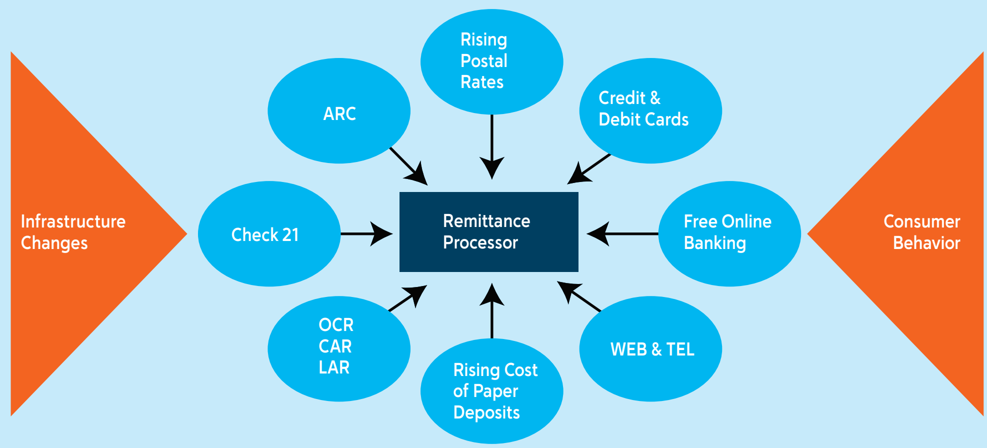
The proliferation of bill payment options for consumers and fundamental changes in the U.S. check clearing infrastructure are fueling an accelerating migration from paper check to electronic bill payments. For an increasing number of billers, acceptance of recurring card payments, ACH check conversion (e.g., ARC, WEB) and rapidly maturing Check 21-based image clearing systems have pushed paper-based remittance processing toward an economic ‘Tipping Point’ where outsourcing is more attractive than updating their in-house operations. As consumer bill payment behaviors change, most in-house retail lockbox operations have experienced declining check volumes and rising costs per item. In this environment of declining volumes, it has become increasingly difficult for in-house lockboxes to obtain the capital investment funding needed to purchase newer and more robust RP equipment and software.

In-house lockbox operators will experience their own ‘Tipping Point’ when they can no longer realize economies of scale, as paper item volume growth is captured by electronic payment methods. As paper check volume declines, an increasingly diverse payment mix adds to the complexity of managing and supporting multiple processing systems needed for integrating electronic payments. For many shops, their last technological refresh occurred during Y2K preparations nearly a decade ago. Now, equipment is nearing the end of its economic life and cannot easily be upgraded to generate Check 21 Image Cash Letter (ICL) and ARC conversion files. The confluence of these factors is leading many to consider migrating some or all RP activities to third-party providers.

The Stressors: Market Trends and Volumes

Changing consumer behavior and infrastructure creates stress and uncertainty for lockbox managers, who must determine appropriate solutions for their company's needs.

Figure 2. Stress Factors Affecting Remittance Processors

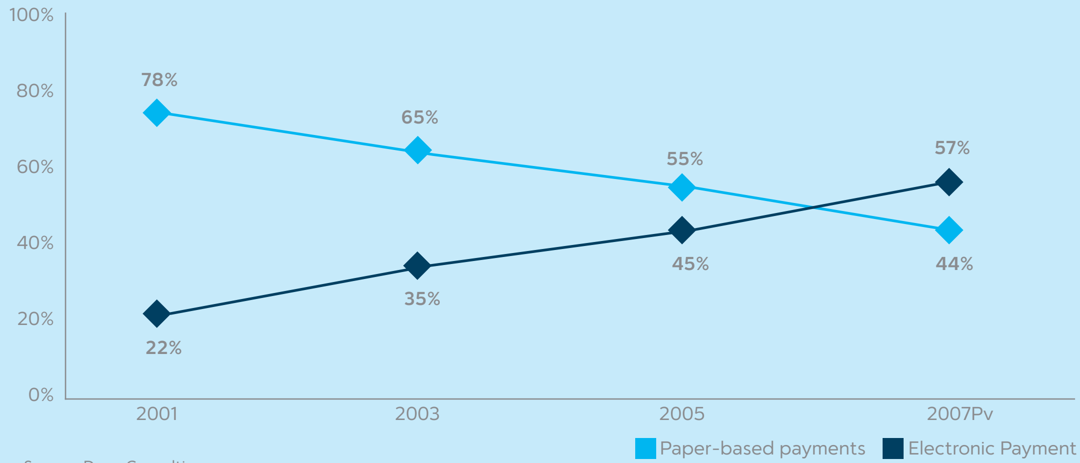


Changing Consumer Payment Preferences

Decision makers may find it useful to review industry volume trends and statistics, particularly those reported in the Federal Reserve Bank of Atlanta's Retail Payments Study (see www.frbservices.org/files/communications/pdf/research/2007_payments_study.pdf). The introduction and adoption of electronic payment such as ACH, credit cards and debit cards have fueled a rapid and dramatic transformation of the U.S. payments landscape. Paper-based bill payments are steadily being replaced by an expanding array of electronic payment methods, and consumers have shown a clear preference for more convenient alternatives at the point-of-sale and, now, for bill payment. ACH payments have experienced strong growth as online bill pay and ACH eCheck conversion programs continue to expand.

As consumers become more comfortable with using new technologies and applications, electronic-based bill payment methods have become preferable to paper. Dove Consulting's 2006 Consumer Payment Preferences Study reported that paper-based bill payment methods were projected to fall to a 44% share in 2007, down from 78% in 2001. The study also found that 45% of household bills were paid with electronic methods, a nearly 40% increase from just two years prior.

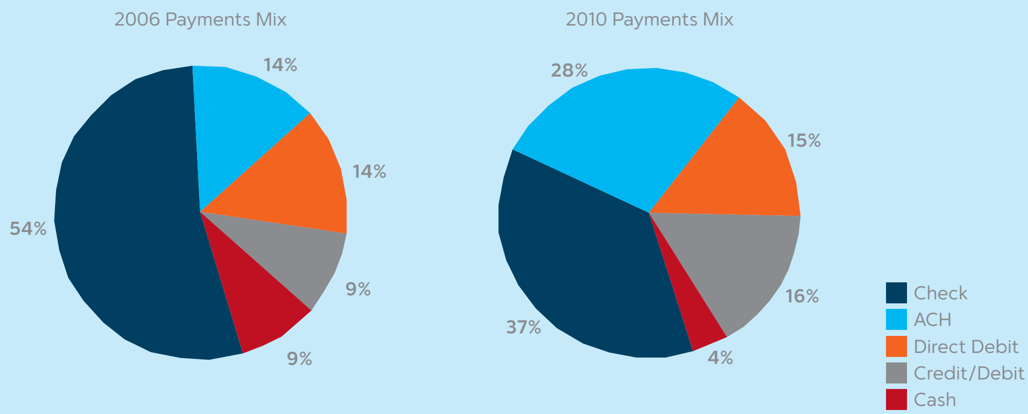
Figure 3. Paper-Based Bill Payments as Percent of Total



Source: Dove Consulting

Consistent with this research, a study by the CheckFree Corporation reported that electronic bill payments surpassed paper payments among consumers in 2006. Large billers in the credit card and telecom industries reported similar statistics; their paper check bill payment volumes have declined to the mid-40% range. This consumer adoption trend will likely continue unabated. Gwenn Bezard of the Aite Group predicts that the percentage of bill payments made by paper checks and money orders will decline from 54% in 2006 to 37% in 2010.

Figure 4. Distribution of Payment Methods, 2006 vs. 2010



Source: Aite Group

Infrastructure Changes Requiring New Investments

Rapid changes in the payments landscape and the proliferation of payment methods are putting pressure on remittance processors to manage their increasingly complex operations with limited resources. Per item costs are beginning to rise due to declining volumes, creating a challenging business case for investing in new systems needed to support in-house operations. Investment is necessary to achieve needed cost savings, but the new payments environment has made it difficult to justify the capital outlays.

Realizing the benefits of ARC and Check 21 ICLs requires extensive system upgrades and process changes for lockboxes, while continuing in-house operations in their current state will necessarily result in declining paper item volume in the near future.

CFOs face the decision to either continue processing remittance in-house or outsource operations to a third party. In-house operations will require additional investment in systems to capture the ARC and Check 21 benefits, but this may lead to higher per item costs as volume falls. Meanwhile, outsourcing will become increasingly attractive if they can retain control of key customer-facing activities and convert fixed monthly operations costs with rising per item costs into a fixed cost per item expense that is easier to plan and to budget.

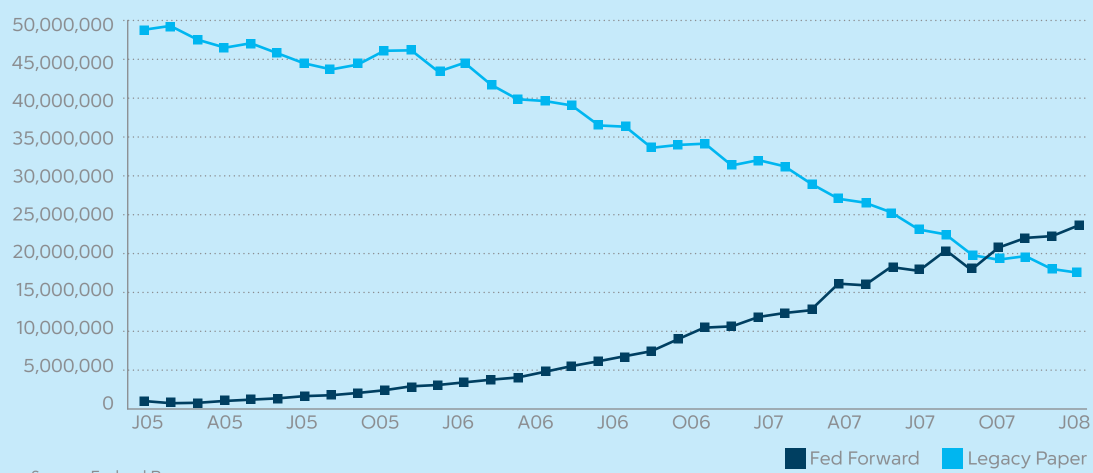
The choice is one that organizations are reluctant to make. It can easily take a year to select an outsource provider and to move the work into their lockbox facilities. After making the initial decision to outsource, companies must also allocate approximately six months to evaluate and to select a vendor, and an additional six months to upgrade or to switch over. While this decision can be difficult for organizations, the supporting evidence clearly shows that the urgency and intricacy of remittance processing requires organizations to decide on a course of action for this new payments environment.

Check Volume Trends

The total number of paper checks written declined at an annual rate of 4.1% between 2003 and 2006. If this trend continues, check volumes could fall to 28 billion by 2010. The rate of decline alone is manageable, but seismic changes are occurring in the paper check clearing world. In December 2007, 57% of the Fed's check volume at collecting banks used image or substitute checks. Fred Herr, a leader of the Fed's Check 21 team recently reported that in February 2008, 60% of checks received by the Fed for clearing were presented as images. He estimates that the percentage will reach 75% by December 2008 and that by 2010, 90% of checks will be forwarded and settled as images—no paper items or Image Replacement Documents (IRD).

In September 2007, the Fed reported clearing as many checks images as paper items. As large banks switch to image clearing, one analyst estimates that legacy paper item volumes could decline by as much as 50% during 2008. With so few legacy paper checks remaining to be cleared, item fees will rise and availability levels will decline at an accelerating rate. By 2009, there may not be enough paper checks remaining to justify the remaining infrastructure.

Figure 5. FedForward vs. Legacy Paper Collection Daily Volume Trends



Source: Federal Reserve

The implication for lockbox operators is that Check 21 ICLs have now reached critical mass, as costs for image deposits are headed down and paper deposits expected to increase sharply for the foreseeable future. For non-bank lockbox operators, the business case for investing in new Check 21 systems is not as clear, since they can leave the image clearing investment to their depository banks. However, the ability to provide the properly formatted file to the ODFI serves as a reasonable and efficient solution.

First and second generation image transports still function, and with lower volume, work can be completed by existing cut-off times with minimal holdover. However, Check 21 is disrupting cash letter cost and float equations. Banks are allowing later cutoff times for check deposits and ACH files. Overlaying the new Remote Deposit Capture options, depositors are revaluating the number and timing of their daily deposits to maximize funds availability. However, for most operations, adding Check 21 and ARC capabilities will require significant investment to replace equipment and image processing software and may change their hours of operations.

Check 21 creates an opportunity for improving the function of lockboxes by reducing float and simplifying operations. However, these changes also imply that traditional batch methods and the geographic dispersal of multiple sites will be harder to realize internally. Lower image clearing fees and better availability schedules have improved the business case for Check 21, sparking greater interest and implementation. However, capitalizing on the benefits of Check 21 requires a strategic overhaul of fundamental operations and organization. Of specific importance to remittance processors, the Fed is making three changes which directly impact lockbox economics:

1. Convenience

As a result of declining check volumes, the Fed has undergone extensive consolidation of its check processing sites. It has already downsized from 45 paper check processing sites to 18 and plans to further consolidate into four sites by 2012.

Figure 6. Federal Reserve Check Processing Consolidation

Source: Federal Reserve

2. Availability

Lockbox payments generally have a lower percentage of local items, so most items must travel to out-of-district banks for clearing. As paper takes longer to travel for clearing, availability of paper items will continue to decrease as transportation costs increase. In response to eroding economics, billers are confronting difficult decisions to either invest in new systems to support ICLs, ACH and cards, or to outsource their operations. The Fed has announced that they are reducing the number of Check Relay courier jet flights and at some point may turn to the USPS mail for paper check transportation. These changes will slow down the funds availability schedules for paper check items by days, tipping the balance toward ICLs which are approaching same day availability.

3. Pricing Incentives

The Fed's pricing structure charges less for image items and much more for paper items, usually more that twice that of image items. For 2008, the Fed announced a set of new prices to encourage image clearing:

- 12.5% increase in fees for forward collection of **paper checks**

- 10.3% increase in fees for collections with **substitute checks**

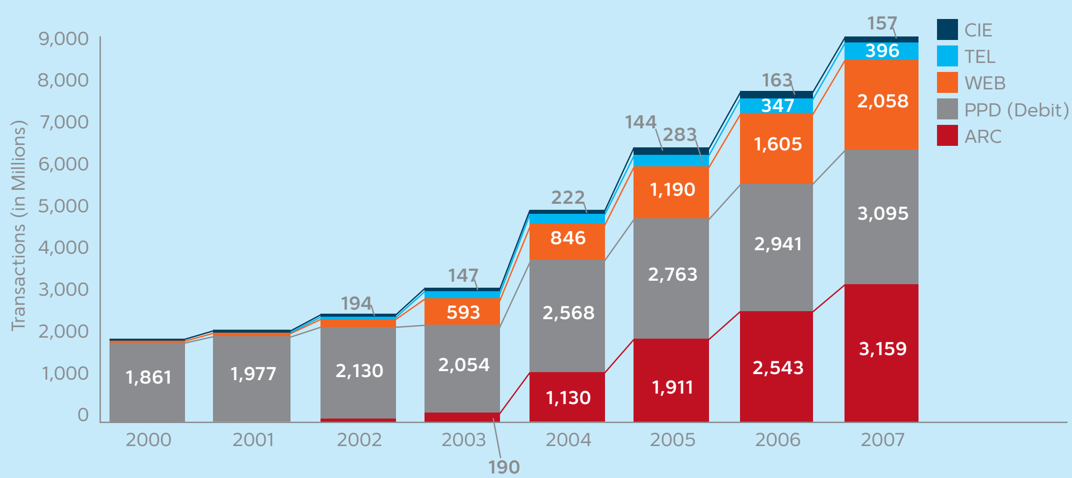
- 3.2 % decrease in fees charged for checks **cleared as images**

ACH Growth is Displacing Bill Payment Check Volume

ACH check conversion often costs billers less than $0.04 an item, which is less than the cost of encoding and depositing paper checks. These cost savings and other factors have fueled the rapid growth of ACH for consumer bill payment from approximately 2 billion payments in 2000 to almost 9 billion in 2007. In 2007, over 3 billion checks were ARC'd. Additionally, recurring and one-time ACH payment methods, such as PPD debits and WEB transactions, eliminate the need for check writing and mailing payments to lockboxes, displacing another 5 billion checks that might otherwise have been processed at a retail lockbox.

For billers, each new eCheck application erodes paper check volume and usually adds more complexities with special rules that companies must follow as they manage A/R posting, exceptions, and bank reconciliation.

Figure 7. ACH Bill Payment Transaction Volume



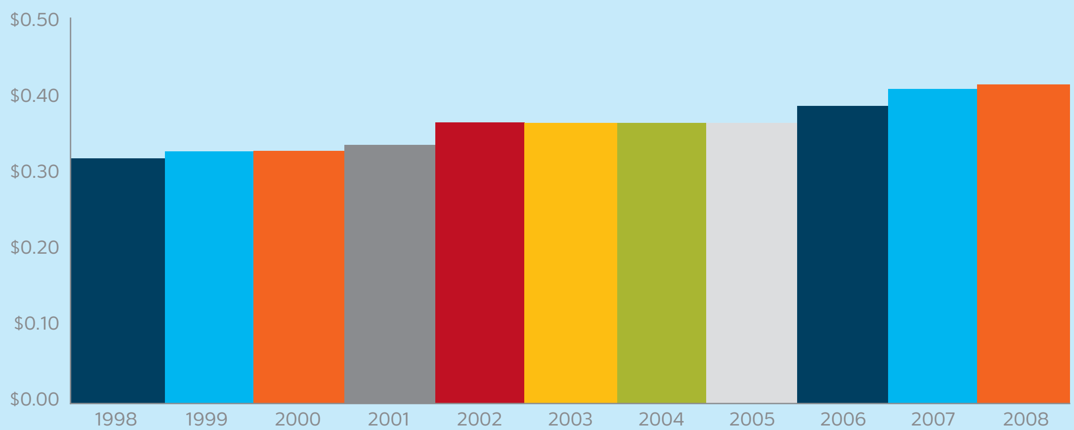
Source: NACHA, Dove Analysis

Online Bill Pay Pricing Driving Consumer Change

Biller websites and financial institutions have been promoting 'free' online bill pay to attract and retain retail customers. This has encouraged consumers to utilize ACH and card-based payments rather than mailing checks to lockboxes.

For consumers, the benefit of 'free' online bill payment is direct. In contrast, the U.S. Postal Service has steadily increased first-class postage rates. For a typical household, sending all bill payments via mail with $0.41 stamps (soon to be $0.42) would cost $6.21 in postage each month, amounting to $74.54 per year. With rate hikes likely to continue for the foreseeable future, the value proposition for consumer online bill payment will continue to improve while paper payments deteriorate.

Figure 8. First-Class Mail Postal Rates



Source: United States Postal Service

Outsourcing Rationale

Need for New Technology

The majority of lockbox operations last refreshed their technology almost ten years ago, and the equipment has begun to deteriorate and require more maintenance. Most in-house lockboxes are using imaging transports and systems that predate the passage of Check 21 and ARC. The implementation of image archiving was done primarily with CD-ROMs. While the benefits of new image capture systems are appealing, implementation requires significant investment of resources that may not be available. Nevertheless, for lockboxes, technological updates are necessary in order to support electronic check processing.

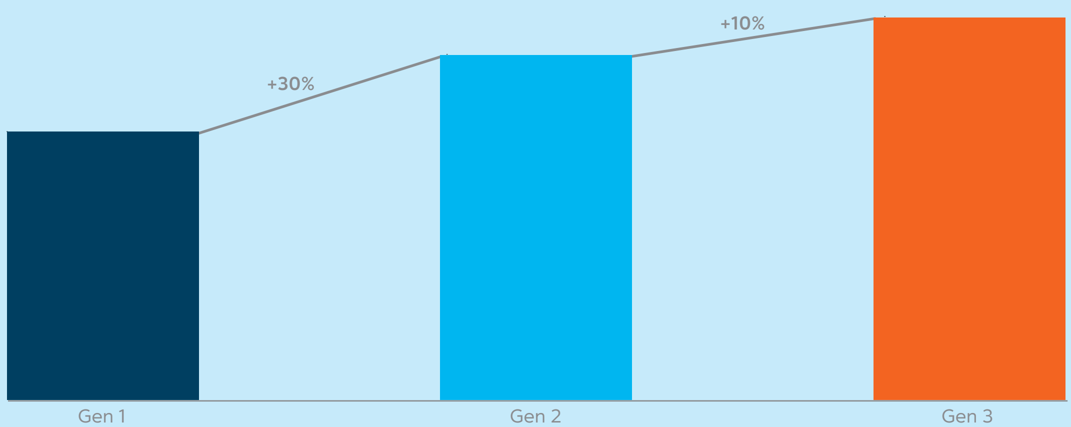
Before procuring a new IT-centric system, most organizations must first establish the scope of system requirements and determine the capacity needed. Then they would need to develop a capital budget request detailing the amount of investment needed, rationale for the effort articulated, labor savings estimated, and anticipated ROI or payback period analyzed.

Challenging Business Case

But what happens when volume is expected to decline steadily over the capital investment analysis timeframe, and there is a risk of needing to write off stranded or obsolete assets with uncertain residual values? This is new territory for organizations and has led some to shorten the estimated useful life for RP systems from seven years to as few as three, raising the required savings to achieve an acceptable return on investment.

Before online bill payment arrived on the scene, lockbox operators could easily justify the acquisition of labor saving second-generation equipment for extracting mail; advanced OCR technology could dramatically reduce the amount of labor required in a lockbox as the systems can 'kill' up to 70% of payments without human intervention. New systems could boost productivity by more than 30% from first-generation 'read and key' systems, and those durable systems were built to run for decades. However, for RP shops that have already benefited with big savings from 'read and key' to second-generation systems with powerful CAR/LAR engines, the 10% productivity gain from upgrading to third-generation systems with ARC and ICL capabilities is not as dramatic.

Figure 9. Estimated Productivity Gains by Generation



Source: Dove Analysis

Need to Reduce Costs

In-house lockbox operations are being squeezed by equipment that is nearing the end of its economic life, labor costs that are rising 3% to 5% annually, and declining monthly paper item volumes. These converging cost pressures make it harder to create the compelling business case needed to get funding for a technology refresh. Unless an in-house RP operation is picking up volume from new customers through mergers or their company's rapid growth, there is limited potential for increasing item volume. The steady 2% to 6% decrease in annual volume that most lockboxes have experienced makes it difficult for the improved productivity gains achieved from third-generation RP systems to offset the additional investment costs.

For many mid-sized in-house RP shops. there will be a net negative financial impact because they will not recoup the investment as easily as in that past. However, if no action is taken, per item expenses will inevitably increase as overhead is recovered over lower monthly volumes. Given this dilemma, it is no longer a matter of whether most in-house operations will consider outsourcing but rather how soon they will do it.

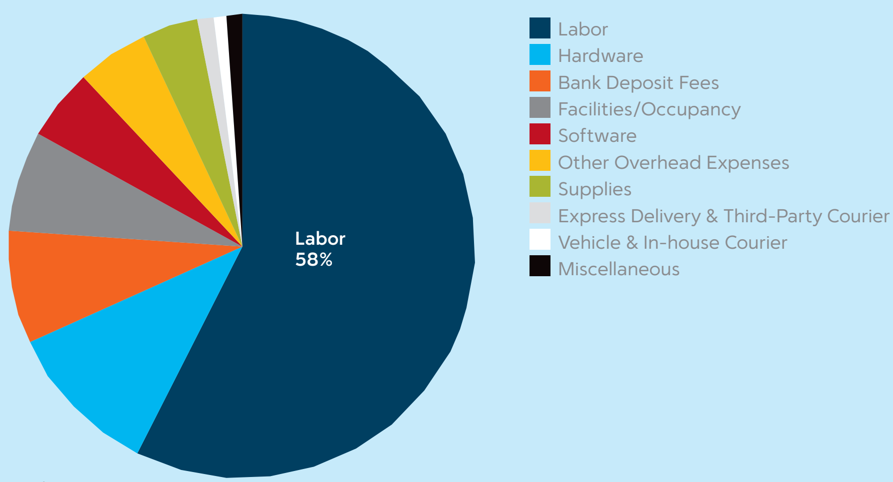
Of course, what they may choose to outsource will depend on each organization's mix of consumer and business customers. Organizations with mostly B2B customers may choose to update their systems to support automated mail extraction and improved data capture by acquiring updated full-page scanning and/or by adopting more wholetail-oriented systems. According to the Fed, there are approximately 8 billion B2B checks being sent each year. B2B volumes are declining at a slower pace than consumer lockbox payments and have a higher dollar value. This indicates that business checks will continue to be an increasingly important source of lockbox volume. Although B2B checks are more challenging to convert into ACH payments, the adoption of wholetail techniques should provide opportunities for growth and value-added image-based services.

What to Outsource

During this transitional period, organizations must examine their priorities, determine which activities are core to their business strategy, evaluate the value of business processes, and provide competitive advantage. For many, certain activities can be performed faster, better, and cheaper through the use of third parties that specialize in tasks such as mail sorting, opening, imaging, and preparing paper items for deposit or ACH conversion using ARC or BOC. A few minutes of work on new high-speed mail opening and image extraction equipment can replace hours of labor-intensive extraction and read-and-key work at low volume in-house lockboxes. This allows companies to free internal staff to focus on core business activities and to extract the benefits without devoting significant resources to performing these tasks in-house.

The 2005 Remittance Processing Benchmarking Study indicated that labor accounts for 58% of a non-bank lockbox's expenses.

Figure 10. Monthly Operating Budget Mix for Non-Bank RP Sites



Source: TAWPI/Dove Consulting, 2005

Although labor rates differ by activity, 68% of paid hours were spent performing four tasks: Mail Prep, Extraction, Keying, and Balancing. These capture-and-keying activities can be readily and efficiently performed by an outsourcer. Moreover, new availability policies for ARC and Check 21 ICLs have created an opportunity to extend cut-off times.

Table 1. Paid Hours by Activity (Per Site)

Activity	Percentage of Paid Hours	Cumulative
Mail Prep	5%	5%
Mail Opening	31%	36%
Keying	28%	64%
Transaction Balancing	4%	68%
Encoding	6%	74%
Sorting	0%	74%
Deposits	4%	78%
Cash Letter	0%	78%
Account Reconciliation	1%	79%
Exceptions Research	7%	86%
Posting	1%	87%
Return Items	1%	88%
Bank Advices/Investigations	1%	89%
Address Change	1%	90%
Other	9%	100%
Total Paid Hours	**100%**	**100%**

Source: TAWPI/Dove Consulting, 2005

Declining Volume and Loss of Economies of Scale

Businesses must recognize that volumes must offset the costs of overhead and investment in order for in-house operations to be worthwhile and sustainable. The late John Black, former Chairman of the Board of TAWPI and the first chairman of its Payments Capture and Clearing Council, observed, "[I]t comes down to scale. For businesses with less than [1 million per month in volume], the overhead is much higher and, of course, less economy of scale." Under these circumstances, outsourcing may provide greater value than continuing in-house operations for remittance processing.

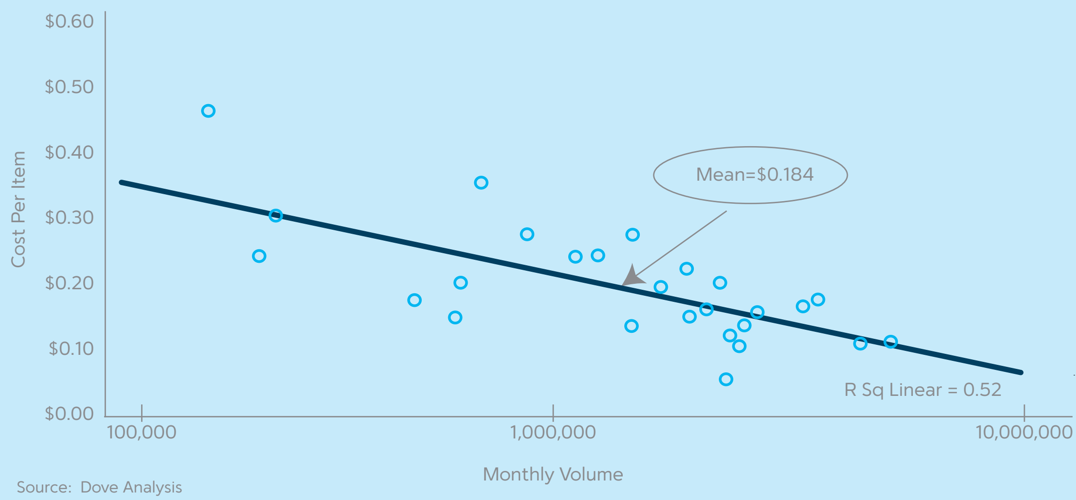
For small to mid-sized companies, this means that outsourcing may be the more viable option, given their comparatively low volumes and high costs. It has been estimated that approximately half of these organizations have outsourced RP activities to third parties, with the other half retaining in-house operations. However, with volumes in a state of decline, this balance will likely tip toward outsourcing as companies decide that diminishing volumes cannot justify the cost of keeping operations in-house.

In an environment where volume is declining, outsourcing allows customers to get both the benefits of new technology and a more predictable cost per item. Thus, companies need to realistically assess their current and future volumes when deciding whether to continue in-house RP operations or to outsource to a third-party provider.

In-House Remittance Processing Cost Curve

Figure 11 shows the relationship between per item costs and monthly volume for 25 in-house lockbox operations from the most recent benchmarking data available. Each data point represents an organization's reported cost per item and monthly volume. Together, they show that per unit costs decrease as volume increases and conversely increase as monthly volume decreases, with a mean cost of $0.184 per item. The blue regression line shows the statistically significant relationship between per item costs and monthly volumes (r^2=52%). The curve shows that as an average lockbox's volume declines, the per item costs will increase; for every 10% decrease in monthly volume, per item costs will increase by approximately 2.7%, without factoring increases in labor expenses or new equipment acquisition costs.

Figure 11. In-House Lockbox Cost per Item vs. Monthly Volume



Source: Dove Analysis

2008 Should Be a Big Year for Outsourcing

Evidence suggests that 2008 will be a busy year for outsource providers as in-house shops evaluate their strategy for obtaining third-generation image capture technologies to support ICLs, remote keying, and improved ARC decisioning and conversion rates. This will lead to an abundance of Requests for Proposal (RFP) issued by organizations with in-house lockbox operations.

Consider the Big Picture

Organizations often fail to look at the big picture when making the decision between processing remittance in-house and outsourcing. Most look at it from a narrow financial perspective, but there are many factors that should influence the decision, including staffing, customer service, and security. Only by viewing remittance holistically and in the context of the entire business process can organizations make an informed decision.

Although the decision to outsource remittance processing depends on market pressures and a company's individual outlook, the trend toward moving in-house operations to a third party is also a reflection of the overall move toward outsourcing all non-core activities. Increased receptiveness to outsourcing in general makes the business case for doing the same with remittance processing more appealing. Outsourcing these activities may be perceived as an inevitable next step in retooling business operations. John Black suggested that a "CFO may decide to look at the bigger picture of BPO, giving up not only remittance but also many other financial functions."

Outsourcing Assessment

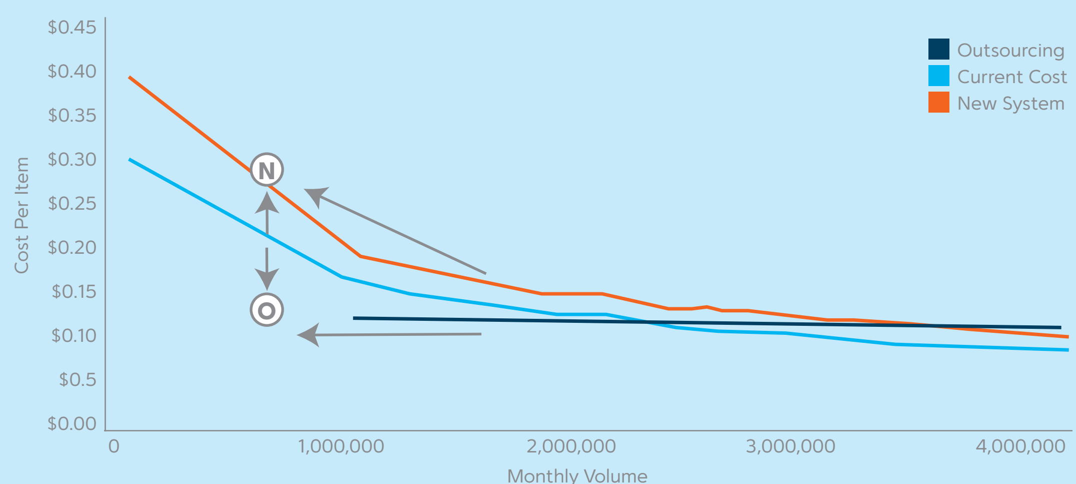
Many in-house billers are examining the costs and benefits of outsourcing all or part of their RP operations to reduce the need for capital investment in the next generation of hardware and software while obtaining the benefits of new image based Check 21 and ACH check conversion systems. In response, senior financial and RP managers are gathering information about their options through Requests for Information (RFIs) and competitive RFPs for two options:

- → Updating their in-house systems
- → Outsourcing their lockbox operations

In general, the largest and smallest lockbox operators are finding that it is most financially beneficial to either invest in new systems or defer the decision. However, mid-sized and large in-house lockboxes are finding that outsourcing can reduce their per item costs while ensuring that those costs can be maintained through contractual terms. In contrast, investing in new systems will increase their per item costs. In some cases, this can be to the point where a new in-house system costs twice as much as what they could have obtained from a third-party lockbox provider.

Figure 12 illustrates the economic equations that are driving remittance processing past its 'Tipping Point' in favor of outsourcing. As volumes fall, an organization can take advantage of market prices to keep per item cost relatively flat by outsourcing. That would let an organization move toward position 'O' on the graph. If an organization purchases a new system, their costs will move toward position 'N,' and if they do nothing, their costs will rise.

Figure 12. Impact of Outsourcing on Per Item Costs



Source: Dove Analysis

As seen in Figure 12, the financial benefits of outsourcing are clear. For instance, most organizations with monthly volumes from in-house retail lockboxes between 400,000 and 2.5 million items will see significant advantages in outsourcing, which would allow them to focus on core business and to relegate non-core activities to a less costly provider.

Outsourcing also allows organizations to mitigate the risk of increased unit costs due to declining volumes in the long-term. By obtaining a fixed multi-year contract, they transfer this problem to their provider and are able to reap the benefits while offloading the financial risk.

Options to Consider for In-House Operations

Maintain Status Quo

Based on industry trends and pressures, continuing in-house operations in their current state appears to be an unsustainable strategy in remittance processing. The number of paper checks received by retail lockboxes is declining at a rapid rate, as consumers continue to migrate to electronic bill payment methods. This will lead to an inexorable annual increase in per item costs.

Add External Volume

Some organizations have been able to grow their own monthly volume by taking on outside work from other lockbox operators. While this is a more viable option than maintaining the status quo, adding external volume also requires additional strategic considerations, some investment, and implementation of new tasks. This will include new costs for sales and marketing, billing, administration, reporting, and customer services, which may outweigh the benefits of adding volume. John Black observed that providing services for other lockbox customers "may help get some incremental business for the smaller operations that were thinking about upgrades, but they are then forced to go through the business case of looking at an upgrade versus outsourcing." This option essentially defers the outsourcing decision for perhaps two to three years.

Adopt a Selective Outsourcing Approach

When considering outsourcing, organizations must identify what matters to them and what can be seamlessly outsourced to a third party. For most organizations, activities that ultimately affect their customers, namely exceptions handling, are of highest value. Lower-value activities such as mail extraction, capture, and data entry comprise a large percentage of labor hours and may be the most suitable option for selective outsourcing because providers can perform these tasks at higher efficiency and at lower cost. Online exception processing allows the biller to maintain control of the sensitive areas that affect customers. Tasking the outsourcer with activities that yield the biggest rewards from economies of scale also frees managers to focus on high-value activities that help retain customers and enables organizations to maintain control over the operations that matter most.

Benefits and Considerations

Each organization should evaluate its alternatives in light of the benefits and considerations outlined below:

Benefits of Outsourcing

- → Reduce cost of operating and maintaining RP systems and technology
- → Utilize new technologies as they become available (e.g., Check 21 ICLs, ARC, Image Archiving, etc.)
- → Transfer challenges with staffing, systems conversion, and training issues to a specialist
- → Minimize risk of increased per item costs as volume decreases
- → Provide business recovery and contingencies for facility service interruptions

Considerations

- → Diminished control: Are all of your items being processed the same day, every day?
- → Big Fish/Little Fish: How responsive will your provider be to your needs?
- → Willingness to support selective outsourcing and service level agreements
- → Exception processing: Do you and your provider agree on the definition of 'exception'? Do they have the ability to let you maintain control?
- → Pricing over the long-term
- → Stability and continuity of outsourced providers
- → Process for changing procedures and services

Ultimately, the decision to outsource should rely on considerations that take into account all factors important to a company's strategy. Identifying the outcomes, maintaining realistic expectations, and, most importantly, effectively communicating these issues to potential providers also increases the likelihood of a beneficial relationship. When companies approach decision-making holistically, outsourcing can provide great value and yield success for a company.

Call to Action

Create and Evaluate a Payments Migration Strategy

New rules and payment methods are added every year, and, as a result, the complexity of RP operations has increased exponentially. The changes occurring in remittance processing—and the payments industry at large—make it absolutely essential for RP managers to act as key players in the development and execution of their organization's payments strategy. As consumers and businesses increasingly utilize multiple payment methods, there will be strategic and competitive benefits for organizations that can effectively coordinate and manage this critical aspect of customer interactions and relationships.

Questions to Consider

- How much longer will customers continue to pay with paper checks in large volumes to justify new systems and in-house operations?
- How will you continue to absorb increasing unit costs year after year?
- What is your strategy and how will you react to the myriad of pressures in this new payments environment?
- What is your organization doing to prepare as the lockbox world reaches a very different 'future-state'?
- Will you be able to capture the benefits?
- What are you waiting for?

First Data

A Global Leader in Electronic Commerce

First Data powers the global economy by making it easy, fast and secure for people and businesses around the world to buy goods and services using virtually any form of payment. Serving millions of merchant locations and thousands of card issuers, we have the expertise and insight to help you accelerate your business. Put our intelligence to work for you.

About Dove Consulting

Founded in 1981, Dove Consulting, a division of Hitachi Consulting, is a Boston-based consulting firm specializing in financial services. A leader in developing retail payments, distribution, and customer strategies, the group has performed payment strategy work with seven of the Top 10 U.S. banks, credit unions, major payment networks and processors, and government entities.

Dove's value proposition—deep expertise for immediate value, sincere collaboration with clients, and the delivery of clear results—has enabled the firm to become a highly valued and trusted advisor to leading financial institutions, networks, processors, and other providers all over the world.

Client consulting work at Dove is supported by an ongoing commitment to industry research. The firm's primary research has addressed payment trends related to consumers, retailers, ATM deployers, card issuers, businesses, government agencies and remittance processors.

About First Data Services/REMITCO

REMITCO, a First Data company, is the leading provider of third-party payment processing in the country, operating a seven-site network designed to reduce mail float and time in process. REMITCO offers a comprehensive payment processing solution that provides inherent flexibility to manage changes in consumer behavior while taking advantage of advanced electronic functionality.

REMITCO is focused on simplifying the transition from paper to electronics for companies of all sizes in all industries.

For more information, contact your
First Data Sales Representative
or visit firstdata.com.