



Play 21

JOHN DOE 123 SOUTH ST TOWN, TX 12345	1234
11/1/07	
PAY TO THE ORDER OF RETAIL STORE	200.00
TWO-HUNDRED DOLLARS AND NO/100	DOLLARS
COMMUNITY BANK 12345 BANK RD TOWN, TX 12345	
John Doe	
⑆123456789⑆1234⑆123	

Illustration by Randall Nelson



OPERATION ELECTRONIFICATION

THE CONVERSION FROM PAPER CHECKS TO DIGITAL PAYMENTS IS TODAY'S WINNING STRATEGY



Starting in the 1970s, with the introduction of payment cards, banking industry pundits began predicting that we would soon become a checkless society: a society where individuals and busi-

nesses no longer had a need to write checks. Decades after that prediction failed to materialize, the focus shifted from check elimination to check electronification upon the realization that consumers and businesses would always write checks, at least during most of our lifetimes. Still, the industry has seen further unprecedented reductions in paper check volumes and increases in electronic payments since the arrival of the 21st century.



By Viveca Ware

This recap of the current payments game is based on feedback from ICBA's Payments and Technology Committee. The community banker-run group addresses various policy issues affecting the online delivery of financial services and payments, and maintains ongoing relationships with the Federal Reserve System and other public and private sector organizations to ensure an open and competitive legal, regulatory and operational framework. Findings from ICBA's 2007 Community Bank Payment Survey were also included to help determine the next payment play.

GET IN THE GAME

Today the financial services industry is rapidly moving to two-way check image exchange. This migration of payments will take the synergy of all those in the industry, but the driving force of community banks is particularly vital to the check electronification process. The Federal Reserve Banks have a number of Check 21 products, services and resources available to help banks convert paper checks to electronic checks.

Community banks can either jump on board while the tide is still low or struggle against the current once the Federal Reserve completes its long-term strategy of downsizing its check processing sites. Banks that do not make the switch will experience higher item processing and

transportation fees, compressed cash letter delivery and pickup schedules, and will lose their competitive edge.

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percent of the survey respondents plan to implement image exchange by 2009. Forty-five percent of the respondents currently deposit image cash letters, while 43 percent plan to implement the service within the next two years.

This trend among community banks is in line with data collected from banks of all sizes and charter types. Statistics from the Federal Reserve Banks, National Check Clearing House Association and the Small Value Payments Company demonstrate that the number of check images and substitute checks processed are soaring. From June 2006 to June 2007, the number of images and substitute checks received for forward collection grew from 206.4 million to an astounding 734.3 million—a 256 percent increase. The dollar value grew from \$479 billion to \$997 billion. In June 2007 alone, 66 percent of the volume was cleared electronically. As of July 2007, the Federal Reserve Banks reported that over 38 percent of checks collected were deposited in image cash letters.

Moreover, during the last two years, community bankers' perceptions have also changed regarding the number of electronic transactions versus paper transactions processed by their banks. Sixty-eight percent of the 2005 ICBA Community

A Game Plan to Follow

The check electronification game is not over until the final game buzzer sounds. In the meantime, consider these new plays:

- Learn the pros and cons for each check electronification model;
- Understand business case considerations for your bank and your customers;
- Evaluate the costs and benefits of each model;
- Develop a check electronification strategy (doing nothing is not an option);
- Determine how to overcome associated challenges and issues;
- Address risk management issues; and
- Develop education for employees and customers.

Bank Payments Survey respondents believed that their banks were processing more paper checks than electronic transactions. However, only 54 percent of the 2007 survey respondents believed that their community banks were processing more paper checks than electronic transactions—a 14 percent decrease.

Compared to many of their regional and national competitors, community banks are thus far leading in the check image exchange game. But, it's only halftime.

Halftime gives sport teams the opportunity to revisit strategies, successes and failures, and to think about what the second half may hold. Even though a team may be leading, failure to use this time productively may result in a disappointing second half, even a loss.

Community banks should also view this time as an opportunity to prepare for new check electronification game strategies, both defensive and offensive, while continuing the proven check image exchange game plan. Community banks must gain an understanding of the various electronification plays or models to maintain the lead and win the check electronification game. The plays currently include customer remote deposit, ACH Check Conversion and branch capture.

CUSTOMER REMOTE DEPOSIT PLAYS

Customer remote deposit is both an offensive and defensive play. Image-based remote deposit allows business customers to scan paper checks and transmit images to the bank for electronic clearing

percent of the respondents have already implemented customer remote deposit, while 72 percent are planning to within the next two years.

However, community banks should not rely exclusively on image-based remote deposit capture to score in the check electronification game. Now is the time to consider adding ACH Check Conversion applications to the playbook. NACHA-The Electronic Payments Association continues to develop new ACH Check Conversion applications that convert paper checks to ACH debits for clearing and settlement. A competitive suite of remote deposit products should include imaging and ACH solutions to afford customers the flexibility to choose which payment processing method works best for them.

ACH CHECK CONVERSION PLAYS

ACH Check Conversion currently has three plays or models—Accounts Receivable Conversion, Point-of-Purchase and Back Office Conversion—that allow community banks to tailor the product offerings to the needs of their customers.

Billing organizations that receive check payments in the mail are appropriate prospects for Accounts Receivable Conversion, which enables organizations to convert paper checks mailed to lockboxes to ACH debit transactions. An image of the check is archived and the original is stored for 14 days, after which point it is destroyed. Consumers see an ACH debit on their monthly statement that includes the name of the company paid, the check number and the amount.

According to ICBA's Community Bank Payments Survey, 21 percent of the respondents have already implemented remote deposit, while 72 percent are planning to within two years.

and settlement without ever leaving their office. Community banks already recognize the value of a product that provides the competitive edge needed to strengthen existing customer relationships and allow for the potential consolidation of various banking relationships, all while broadening their geographic reach to attract new customers.

According to ICBA's Payments Survey, 21

The ACH Check Conversion model, Point-of-Purchase, is specifically designed for retailers. Using this conversion model, the cashier scans a consumer's check and returns the check, stamped "paid," to the consumer upon checkout. The scanned check information is then used to create an ACH debit to the consumer's account. Consumer authorization is explicitly required.



The most recent ACH Check Conversion model, effective on March 16, 2007, is Back Office Conversion. This model allows retailers to accept paper checks at the point of purchase and convert the checks into an ACH debit during the back office processing. By handing over the check, consumers consent to their checks being converted into an electronic payment.

banks can take full advantage of two-way check image exchange and size up the opportunities to add new plays to their check electronication playbooks. **ib**

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MORE INFORMATION

Visit ICBA's Payments Resource Center at www.icba.org/goto/paymentsresources.

BANK OF FIRST DEPOSIT PLAYS

In their role as banks of the first deposit, community banks must also devise effective moves to ensure that cost-effective and efficient check electronication strategies are in place. Community banks have earned glowing analysts' reviews for their check-image-clearing strategy. These plays should include an evaluation of the check image capture at the branch or teller line.

Currently, another ACH Check Conversion play, known as Deposited Check Truncation, is in development by NACHA. Deposited Check Truncation would allow the bank-of-first deposit to convert over-the-counter paper checks to ACH debits for clearing and settlement. It's not a matter of *if* this play will make its debut, but *when*.

The check electronication game will not end with the industry's embrace of check image clearing. Remember, it's only halftime. Community