Emerging Trends in Straight-Through Reconciliation

For an increasing number of payment factories and SSCs (shared service centres) that already achieve high rates of STP (straight-through processing), optimised expense savings and efficiency gains, this article asks what many organisations want to know across the cash management and liquidity spectrum: what’s next on the agenda?

Many companies reaching this position have turned their attention to other costly operational activities such as statements reconciliation. Companies anecdotally reporting auto-reconciliation rates of 20% or 30% of bank statement entries are struggling with largely manual processes to complete the task. Their new target is achieving high rates of STR (straight-through reconciliation), built on the greater automation of the statement-matching process, and significantly reducing the entries left to manual reconciliation.

Improving STR rates not only yields further process efficiencies and savings, but also helps best-in-class SSCs to achieve greater effectiveness by delivering real value-added outcomes to their businesses. For example, better STR rates help drive quicker cash application, reducing DSO (days sales outstanding) and freeing up customer credit lines for more business.

Citi recognised the new focus on STR several years ago, and responded with a package of statement enhancements and specialised reconciliation tools to help customers realise their goals in this area. This is now an opportune moment to reflect on recent experiences and pick out the trends that point to future development.

Reconciliation best practices
Spend any time speaking to different companies about their statement processing and reconciliation needs, and you soon appreciate how these can vary by department (treasury, accounts payable, accounts receivable), by local in-country practices and even by system (e.g. TMS or treasury management systems versus ERPs or enterprise resource planning systems).

There are several ways of looking at these contrasting needs, each of which brings a different understanding of how to approach the issue.

Developing understanding of reconciliation needs

- Improved Visibility of Account Balances
- Accurate Invoice Matching
- Quicker Cash Application
- Reduced Manual Intervention
- STR Rates Up!
Financial versus operational reconciliation

A key part of the morning ritual in any TMS is the updating and reconciling of cash positions across company bank accounts via a daily upload of electronic bank statements. From here, treasurers build an accurate picture of liquidity and working capital, investment opportunities and funding requirements for the day. This financial reconciliation focuses on balances and net credit and debit movements across the accounts.

By contrast, ERP systems need to operationally reconcile payments and collections generated by the respective purchase-to-pay and order-to-cash cycles of the business. This level of reconciliation is more detailed and information-hungry, requiring transaction references, remitter identification and remittance information delivered via the payment networks and banks.

Proclaimed rates of statement reconciliation are generally very high for a TMS but much less so for an ERP tasked with operational reconciliation. Companies looking to raise STR rates are typically those that recognise the underperformance of their operational reconciliation, and so they seek improvements in statement content for their ERPs.

Payables versus receivables

The operational reconciliation of payments and receivables is traditionally conducted separately, applying different reconciliation logic to the debits versus the credits on a statement. Payments reconciliation recognises that a payment run is a controlled activity against which there is a clear record in the ERP of what debit amount should appear on the statement and on which date. Finding a match for a statement debit entry should therefore be quite straightforward.

Conversely, statement credits, representing receivables from incoming payments and cheques, present a tougher challenge. Additional remittance information might arrive by separate means, in different formats and even at different times than the bank statement. Achieving a three-way match between statement credit entries, remittance information and open invoices in the ERP/sales-order system will require sophisticated techniques with effective automation relying heavily on accurate and complete remittance information.

Payments reconciliation is clearly the low-hanging fruit, and companies have invariably focused on improving STR for payables first. Receivables reconciliation requires more complex processing, spawning several specialist vendor products in the market that employ powerful rules-based matching engines to improve automated reconciliation.

Outgoing versus incoming transactions

With the increasing popularity of direct debits as a method of collection, companies can initiate receivables as they do payments, meaning that receivables can also be reconciled on statements as payments are. By initiating a collection run as a controlled activity on the ERP, there will again be a clear record on the system – this time for a known credit – that should appear on an account statement on a given date. Reconciling a direct debit can then be as straightforward as reconciling a payment.

Reconciliation best practices can therefore be seen in terms of outgoing transactions, initiated by the company versus incoming transactions initiated by its counterparty.

STR Best Practice

**Outgoing Transactions**

- STR-savvy companies assign unique transaction references to each and every transaction (both payments and direct debits).
- Transaction references, also known as End-to-End IDs, should not exceed an agreed length that banks can support on statements.
- Common practice is to limit references to max 16 chars, in line with MT940 tag 61, subfield 7 (Reference for the Account Owner).
- Bank account statements should report each transaction as an itemised entry to include companies’ transaction references.
- Transaction references can also be used to uniquely identify transactions on any reject response file or payment status report.
- Recognise when batch booking entries are more appropriate, e.g. payroll payments where confidentiality needs to be respected.

**Incoming Transactions**

- Reconciliation logic must allow for different levels of remittance info being supported by different payment clearing systems.
- Remitter behaviour is key; STR-savvy companies educate their remitters on what info & references should accompany payment.
- Tailoring remittance instructions to respect local clearing and reporting limitations will help address data truncation concerns.
- In some markets remitter account numbers are considered confidential, and cannot be reported in full on statement entries.
- Consider products and services that match externally collected remittance info to bank statement entries. Check whether these can automate matching in non-BAU scenarios, e.g. aggregating invoices, split payments, partial receipting, credit notes.
STR and enriched statements

Conventionally, companies receive and load the same daily electronic bank statement into both their TMS and ERP systems. Yet for companies striving to improve STR rates on their ERPs, there is a growing acceptance that different types of statements, maybe even formats, are needed to better address the different information needs of TMS and ERP systems.

Some banks have responded to this by offering separately generated enriched statement files for ERPs alongside their standard SWIFT-delivered MT940 and MT942 reports for TMS consumption. The enriched statements offer better support of itemised transactions, detailed remittance information and customer end-to-end references. As banks develop greater sophistication in their file-based ERP-oriented statements, the gulf between these and standard TMS-oriented statements grows, giving companies real choice to match their reconciliation needs.

A typical “differentiated” statement solution would feature:

- The timely delivery of standard SWIFT MT940 statements plus real-time MT942 intraday reports over the SWIFTNet FIN channel to a company TMS.
- The delivery of enriched file-based statements into one or more company ERP systems via a host-to-host internet protocol or the SWIFTNet FileAct channel.

STR and SEPA

Given that key parts of what companies look for in account statements depend largely on what information can be transported through the payment-clearing systems, you might ask if there are payment methods that support STR particularly well.

SEPA is an excellent example of a payment scheme that has incorporated many of the information requirements needed for efficient reconciliation, like:

- The need for initiating parties to have unique transaction identification embodied in the end-to-end reference.
- The need for reasonably generous 140 characters of remittance information for receiving parties, supported with options for structured (tagged fields) and unstructured (free text) forms.
- The need to include distinct party identifier fields, covering debtor, creditor, ultimate debtor and ultimate creditor roles to help support POBO (payment-on-behalf-of) and ROBO (receipt-on-behalf-of) scenarios.

Some communities, notably the Finns, have implemented a SEPA AOS (additional optional service) to further enhance the amount of remittance information that can be passed with payment, eschewing the standard provision of 140 characters as inadequate.

Well, if “information is king”, could we now expect STR-friendly SEPA to help European companies achieve better reconciliation efficiencies and cost savings than companies operating with less STR-friendly payment schemes? Could Finland, benefiting from an even more STR-friendly AOS, enjoy a competitive advantage over the rest of Europe? And where does that leave UK corporates, tied to an older clearing system that caters for only 18 characters of remittance information?

Levity aside, there is no doubt from recent experience in Europe that the migration to SEPA is leading many companies operating in the region to adopt STR best practices, such as using end-to-end IDs to automate reconciliation.

STR and ISO 20022 XML

If SEPA is having a beneficial impact on helping companies achieve better STR rates, can the same be said of the format that is most closely associated with it: ISO 20022 XML?

In recent years ISO 20022 XML has been very much in vogue, with banks across the globe helping customers re-engineer their payment and direct debit files into this format. In Europe, SEPA has helped drive greater corporate adoption of ISO 20022 XML, yet the camt.053 account statement message has been somewhat lagging behind, despite it being a structurally better format for presenting statement information compared to older formats, such as MT940, BAI2 and EDIFACT FINSTA.

As a universal financial messaging format, ISO 20022 XML has enabled many companies to streamline and standardise their use of payment formats globally, replacing many of the local file formats that corporates used to have to deal with.

However, for electronic bank statements, there has not been the same proliferation of local formats to tackle, and most multinationals have already standardised their reporting on current widely-supported formats, such as MT940. Some banks have also upgraded their more established statements to report the richer data content of newer payment schemes, such as SEPA, just as well as the camt.053.
Ultimately, system support also becomes a major factor, with out-of-the-box availability of ISO 20022 XML still developing, even among some of the more popular TMS and ERP systems.

What can we take away from all this?
Corporate interest in STR rates and statement content in general has never been higher. There is both a growing recognition that statements reconciliation is multi-faceted and a growing understanding of the differentiated needs between financial and operational reconciliation, TMS and ERP requirements, and the different logic needed to reconcile outgoing transactions and that of incoming transactions.

SEPA will have a beneficial impact on STR. While ISO 20022 XML promises the same, it has some way to go to rival the popularity of older formats. Both developments confirm the rising importance of information content as a prime driver of achieving better STR rates.

Banks, like Citi, and system vendors that have recognised this trend in recent years have responded through various product enhancements that today present customers with a richer, more sophisticated set of statement capabilities than ever before.

Transforming the way treasuries do business
So how does a world-leading bank like Citi help leading organisations and institutions the world over transform the way they do business?

Treasury and Trade Solutions
Citi Treasury and Trade Solutions (TTS) offers the industry’s most comprehensive range of digitally and mobile enabled treasury, trade and liquidity management solutions, platforms, tools and analytics, leading the way in innovation and customisation to support its multinational corporate, financial institution and public sector clients.

With the industry’s largest proprietary network, banking licenses in over 100 countries and globally integrated technology platforms, TTS offers deep local market knowledge, expertise and insights to ensure its clients can meet their strategic business objectives.

Find our more
Contact your Citi representative or find us at transactionservices.citi.com.