WHY CREDIT UNIONS SHOULD ADOPT ALTERNATIVE PAYMENT SYSTEM SOLUTIONS

A white paper by

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Executive Summary

When Credit Unions do their respective due diligence and investigate alternative payment system solutions, a myriad of questions and concerns regarding offerings arise. All too often C-level executives hold to the position: “If it’s not broken don’t fix it.” It is no longer prudent to be content with the status quo – options exist.

In recent years, many Credit Unions have studied the inherent value and offerings of corporate Credit Unions against correspondent banks that provide financial settlement services through the clearing of payments (check clearing), ACH (Automated Clearing House), electronic funds transfers (EFT) and ATM transaction services and networks.

To ensure your Credit Union is meeting competition demands and enhancing the member experience, a thorough understanding of existing payment solutions is required. This includes a secure network for deposit, electronic pay, transfer, debit and other financial transactions. After all, this is the life blood of any financial institution. The question is: Is your Credit Union paying too much for these services? The answer the majority of the time is: Yes!

For small Credit Unions, partnering with an industry leader such as United Resources Federal Credit Union (Western Bridge Corporate Federal Credit Union) makes sense. Larger Credit Unions, however, have the resources to go directly to vendors, and there are many vendors offering these payment system services and are ready to negotiate.

The purpose of the white paper is to demonstrate the benefits, pros and cons of investigating available new services. The goal is to streamline operations while being compliant with state and federal regulations. To be clear, there is security and related operational issues to consider as well as costs and investments related to staff and support services. These critical aspects will be addressed in greater detail within this paper.

Gaining a New Perspective

It is no secret that (historically) Credit Unions are not proactive in relation to payment services and this is for good reason. After all, why should a Credit Union second guess the important role the corporates have played up to this point? The process has run smoothly - no reason to upset the apple cart, right? Wrong. The corporate that was needed and trusted for decades is a good option, but not the only option.

Think of any corporate as the middle man added into the chain of necessary financial operations; it is an essential link in payment processes. Therefore any vendor, less the Federal Reserve Bank, is a middle man. The question is: How much value is that middle man adding? This has to be continually reviewed because your Credit Union could be leaving money on the table.

When it comes to ACH and Wire Transfers, for example, on average these middle men do not add much value. Conversely, middle men providing shared drafts and check processing services are adding value. Again, there are pros and cons to explore but the leading determinant is the size of your Credit Union as that determines investment versus savings.

Only recently have progressive, large Credit Unions embraced the idea that it can approach a bank or a larger conglomerate for services so critical to the member experience such as shared drafts, ACH and lines of credit. This requires knowledge, experience and due diligence on behalf of the Credit Union.

For example, significant savings can be realized in ACH and Wire Transfers. Corporate versus the Federal direct cost is approximately a 66 percent savings, or roughly one-third of the price. One Credit Union Samaha Associates worked with recently saved 65 percent based on actual volume. This “switching” is a detailed, involved process requiring an experienced consultant to oversee the cumbersome transition, a process that usually takes four to six months.

This is new ground for the Credit Union industry requiring a learning curve. Credit Unions, after all, are not expected to know all the answers to this process, but we are finding more and more Credit Unions are asking the right questions.

Vendor Outlook

As consultants, we continually look to indicators. Among these are ways in which vendors approach the market. This aspect of the industry changes all the time. In the end, vendors need Credit Unions more so than Credit Unions need vendors. Why? There are so many vendors competing for market share.

When vendor contracts end, more and more Credit Unions are looking at this juncture as an opportunity. We are seeing more Requests for Proposals (RFPs) with enhanced questioning. No longer are contracts simply rolled over. We are experiencing this trend most in the many system conversion contracts we are engaged in.

As a result, vendors are more open and competitive with pricing because they also understand market indicators. To secure contracts, vendors are more flexible when it comes to hardware costs or using existing hardware Credit Unions might have in place. For larger Credit Unions in the process of revaluating existing payment services relationships, opportunities for meaningful change exist.

New Pathways

It is prudent to note the economic conditions facing the industry as a whole. Corporate Credit Unions are forced to enhance and adapt in order to meet the tougher NCUA financial ratio requirements that have been put forth. The biggest issue facing the industry in this respect is that many Credit Unions can no longer easily utilize corporate lines of credit for reasons such as arbitrage or taking advantage of participation loan deals.

When it comes to ACH, for example, a Credit Union follows regulations and has the ability to pull and view a file and then send it to the host system. From a shared draft perspective – image integration with host provider requires Credit Unions to seek vendor providers. Credit Unions are responsible for collections and resubmittals which may require member fee increases. Therefore, it is important to look at the positive and negative increased costs and then compare those findings to savings that could be realized by making the switch.

Oversight and Guidance

This is a complicated process. At Samaha Associates, we encourage our clients to examine all options available to them including corporate offerings because every situation is unique. We handle the detailed RFP process ensuring that the right questions are asked and answered to determine the best approach. We then meet with multiple vendors offering these services including the Federal Reserve. We aggregate information, negotiate pricing and ultimately assist in the selection of the best solution for the respective Credit Union. Next we manage the implementation process.

It is important to note that a Credit Union or a consultant cannot negotiate with the Federal Reserve – what they offer is their bottom-line pricing. Consider the Federal Reserve the bench mark for savings. Every other option will be higher but will still equate to money saved.

While we can't save every client 65 percent, we facilitate significant savings which more than pays for our consulting fee. The majority of our payment systems projects fall between four to six and months. We work on a fixed monthly retainer based on Credit Unions resources and availability.

The majority of our clients that have switched respective payment services have realized a Return on Investment (ROI) within months. Once the system is implemented and goes live, savings are automatic. In some cases, we have completed projects where our client realized savings immediately.

For example, if a Credit Union were to move all systems to the Federal Reserve and they were paying $17,000 for services previously, the fee would decrease by $11,000 and they would pay just $6,000 per month of that initial cost. Keep in mind that if additional staff or services are required, that will offset savings. Even still, savings would be realized.

It is best to begin the discovery process with a firm understanding of all the moving parts associated with payment systems. Formulating a plan of attack and determining which services can be handled without a middle man are among first steps.

Thinking about making the Switch?

Provided below is a checklist of payments systems subject/items to consider when contemplating any transition.

1. ACH Services
2. Cash Services
3. Wires (Domestic and International)
4. Inclearings Processing
5. Lockbox
6. Transit Processing (Branches, Merchant, Home, Mobile)
7. Settlement Services
8. LOC (Variable/Fixed and Settlement)

If your Credit Union is contemplating switching services, consider the services the majority of corporate Credit Unions offer:

1. Loan Participations
2. Bank CD Products
3. Broker/Dealer Partnerships
4. Educational Workshops
5. Transaction & Overnight Accounts
6. Term Certificates

Conclusion

The result of the industry shake up of the five leading corporate Credit Unions has changed other banks' stance of opening lines of credit – they are more flexible. As a result, within the corporate sphere, lines of credit are most often only offered in emergencies. Without increased membership or increasing rates for existing services, Credit Unions are left with a question: Is it time to make the payment services switch?

Progressive Credit Unions should investigate their existing services and examine all options available including corporate and corresponding bank offerings. With the oversight and guidance of seasoned consultants, a system can be selected that will enhance payment services which in turn improves the member experience while saving on the bottom line.

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