



Turning Paper into Profits

Executive Summary

A convergence of issues is driving distributors and their customers to consider a more efficient means of transacting business. While customer/distributor ordering practices in many industries continues to be based upon relationships and increased telephony (with the benefit of Nextel), the invoicing process for a number of companies is undergoing a transformation.

As companies (and individuals) become more comfortable with electronic processes, customers are gravitating to receiving their invoices electronically from their distributors. With the increased use of the internet, many are requesting to receive their invoices via email or are willing to go to a distributor's website to download their invoices. Some are expressing interest in pushing the integration of data even further by having the ability to download distributor billing data directly into their accounting systems.

Progressive customers are recognizing that by receiving their invoices electronically, they can:

- Invoice their customers sooner, thereby improving their cash flow
- More accurately, and quickly, reconcile P.O.'s to invoices to identify potential issues
- Reduce manpower hours devoted to opening, and matching, invoices
- Access additional information and develop customized reporting

Leading distributors, on the other hand, are embracing this trend as "e-invoicing" enables them to:

- Reduce hard costs (paper, postage, toner)
- Reduce manpower expenses associated with invoice processing
- Reduce DSOs and enhance cash flow

While some ERP systems have the capability to facilitate e-invoicing, many distributors are outsourcing this process to a billing service provider (BSP) to leverage their advanced technology, expertise in developing these systems, and support in migrating customers from hard copy invoicing to e-invoicing.

Research Methodology

Over the past year, Allen Ray Associates, Kennedale, TX, and Channel Marketing Group, Raleigh, NC, have researched distributor/customer relationships. In addition to researching customer expectations of distributors and manufacturers, the research looked at the payment process between the entities. Specifically, distributors and their customers were surveyed and interviewed regarding the invoicing process. The research was sponsored by Billtrust.

In July 2007 a survey was sent to over 500 distributors and more than 5000 of their customers across multiple industries. One on one interviews were conducted with 25 distributors and 32 customers. The goal of the research was to probe deeper into the invoicing process. This research was conducted as a follow-up to research conducted in the summer 2006.

Sending Invoices

As distributors have evolved over the years with their ERP systems, many have struggled with ways to issue invoices faster with the hope of being paid sooner. Many issued invoices as soon as material shipped. In fact early techniques included hand delivery of invoices by sales people.

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Today, distributor invoice dissemination practices include:

- Each P.O. invoiced individually, daily, and individually sent via mail, fax or electronically
- Batched and sent daily by mail
- Batched and sent daily via email
- Batched and sent daily via fax
- Batched & sent minimum 2x / day
- Sent weekly via mail
- Sent bi-monthly via mail
- Sent monthly via mail
- Daily via EDI
- Posted on website
- Sending customers an Excel/ASCII file

Customers reported that the methods by which they receive invoices are:

How do distributors currently send your invoices? (Check all that apply)	2006	2007
Mail paper invoices to us as we pick up material	63%	79%
Mail paper invoice/statement 1x/ month	52%	75%
They send us our invoices via fax	34%	51%
They email us with an attachment to print them out	16%	31%
They send them via an electronic file that we print out	10%	11%
They EDI them and we import into our system	1%	6%
Distributor/supplier posts invoices on their website	5%	5%

Note: While the percentage of customers mentioning that they receive paper invoices may seem in conflict with the increased usage of e-invoicing, this represents the reality that customers conduct business with 4-8 distributors, of which only one may offer e-invoicing. Although they may prefer a non-USPS method, today, only a small percentage of distributors offer e-invoicing as a billing option.

It is evident that there is a trend towards fax and e-invoicing. The percentage change among customers from 2006 to 2007 for these categories is significant (from 34% to 51% for faxing and 16% to 31% for email attachments).

A recent posting on www.electricaltrends.com, (a blog co-authored by Channel Marketing Group and Allen Ray Associates), recently mentioned this trend. A distributor made the following comment: *"We started this process about 18 months ago after reading your articles and we were pleasantly surprised that there were a number of our customers who wanted electronic invoices that could be imported into their accounting package. To our surprise, 6 of our customers actually paid us earlier by about 10 days on average."*

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*Posted on
www.electricaltrends.com*

The benefits of e-invoicing were echoed by a representative from a national electrical distributor. One of its divisions is sending a customer their invoices in a QuickBooks file format, via email, nightly, and is being paid in 34 days. They are in the process of identifying other customers to whom they will introduce this service.

With the advent of alternative invoice distribution methods, as responses to this question revealed, customers welcome the opportunity to be able to choose how they wish to receive their invoices from their distributors. From a distributor viewpoint, this can represent an opportunity to differentiate.

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What becomes clear is that a strategic view of the invoicing process can help a distributor improve cash flow, reduce unproductive expenditures and create a more tangible connection with their customers.

Some Common Ground

Historically, many distributors struggled with procedures to manage their Daily Sales Outstanding (DSO's), recognizing that cash flow is the lifeblood of their business. Their customers, on the other hand, recognized that the delivery time of the U.S. Postal Service and the act of contesting invoices could be tools to extend their distributor-issued credit lines.

In its purest essence, the distribution business model is:

- A customer (contractor, dealer, or end-user) orders products based upon credit issued by their distributor.
- The distributor breaks down product into smaller units (from pallets) or places orders with manufacturers for larger orders.
- The distributor sells on credit (the promise to pay, hopefully based upon some security (lien rights) the distributor may have with the customer).
- The distributor "hopes" their customer pays prior to the invoice from their manufacturer coming due.
- Realistically, the manufacturer invoice comes due; the distributor pays the manufacturer and waits to receive payment from their customer. Many distributors try to negotiate extended credit (dating), while others seek bank financing for their inventory and/or receivables.
- The distributor then awaits payment from their customer, enabling them to perpetuate the replacement cycle of inventory and sales. According to the 2005 NAED PAR Report, the average collection period for electrical distributors was **55** days!

Customers are faced with similar cash flow challenges as distributors. Once they purchase from the distributor, their goal is to invoice their customer (while they install products) to collect payment prior to their invoice with their distributor coming due. The challenge for many contractors is that the distributor invoicing process is not as seamless as possible, generating inefficiencies that can inhibit them from invoicing their customers. This traditional "invoice challenge" enables contractors to "buy" time and delay invoice payment.

We see an interesting **confluence of interests** as distributors look to get paid by their customer prior to paying the manufacturer while their customer looks to get paid by their customer prior to paying the distributor.

Through automation of the invoicing process, distributors and their customers can each accelerate the process of getting paid. As the speed of business has quickened, automating processes, like invoicing, is critical to ensuring long-term profitability.

Today, we are seeing many contractors who are generating invoices from accounting software that has the ability to electronically import, and pay, distributor invoices, thus generating channel efficiencies. The most frequently mentioned customer software packages were QuickBooks, Timberline, Dexter-Chaney and American Contractor. The research indicates this trend will accelerate.

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Rising cost

The cost of issuing invoices has risen dramatically. Not only are most distributors issuing more invoices due to their growth, requiring more paper and print toner, but USPS first class rates have increased from 34¢ in July 2000 to a current 41¢, a 20.5% increase. Additionally, consider the increased labor costs (salary + benefits) and overhead costs that companies have incurred over the past seven years. This channel inefficiency becomes amplified when you consider that customers have incurred comparable employment and overhead increases. Of course, the cost of money (cash flow) is a significant issue for many companies.

With a slowing economy, a tightening of margins, and increased workload, many distributors and customers are seeking alternatives to traditional processes. While it is doubtful that a company can quickly convert all of its customers to a new process, a gradual migration from mailed invoices to electronic methods can have significant financial benefits for all parties. Our research shows that customers benefit from a more timely process by being able to reduce their costs, reduce billing discrepancies and improve their cash flow.

As The Channel Ages

Within many distribution channels, change comes slowly. Some of this relates to ingrained processes while some emanates from the age of channel participants.

Based upon interviews, there was a noticeable correlation between the age of a respondent and their willingness to embrace technology and process changes. Many respondents grew up receiving printed invoices in the mail (and if they needed another copy, they went to the distributor). Paper proliferated.

There are some distributors who “believe” that paper invoices are required to prove passage of the title of products. This despite the fact that it is a well accepted business practices that secure electronic documentation suffices to pass title given that appropriate nomenclature is included.

Progressive distributors and their customers who recognize the cost-inefficiencies of this process are seeking new solutions such as synchronizing their data (product information). They are agreeing to new methods of bill delivery and “price tolerances” for their most frequently purchased items. When both parties agree to contracted pricing for selected SKUs, they also agree to manage, and pay, invoices based upon negotiated tolerance parameters. With the implementation of e-invoicing, bills can now be processed with minimal verification, resulting in quick payment and limited personnel involvement.

The slow pace of change is also inhibited by distributors not offering customers what they want. Sometimes this is lack of management knowledge, unwillingness to change, or until recently, the inability of the distributor’s ERP system to accommodate the desired service. According to one customer, “Four of my suppliers offer invoices on their Web sites, but our company can only print PDF files of these documents. What we really want is the ability to import or load all of the distributors generated documents, in particular invoices, into our accounting package,” she says, noting that it would offer the possibility for her company to manage material payables on a price tolerance, or exception, basis. Her example was a ¼% to ½% plus or minus price tolerance per line item and the extended total.

Another customer in Texas provided an example of using advanced techniques to reduce their invoicing costs. This customer receives more than 525 invoices per month from an independent distributor and has an error rate of 0.01%. The key – he imports his invoices and has negotiated a pricing tolerance level with the distributor. He pays, electronically, in full, the last Friday of each month.

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The Matching Game

The research highlights the high level of concern among both distributors and customers relating to billing errors. The largest problem uncovered is inconsistencies between P.O.'s and invoices.

Unfortunately the issue is not limited to a small percentage of invoices. The chart below asked contractors what percent of their distributors' invoices did not match their purchases orders.

% Invoices that Don't Match P.O.'s	
% Errors	% Responses
<5%	65.2%
6-10%	18.9%
11-15%	3.3%
16-20%	5.4%
21-30%	1.1%
31%+	6.5%

As can be seen, errors are rampant in the industry. Thirty-five percent of respondents reported that more than 6% of their invoices have errors, hence generating significant incremental costs (manpower) for contractors and distributors.

Many factors contribute to these errors including backordered items, wrong items shipped, bad descriptions, pricing and quantity.

What % of invoices don't match purchase orders due to	<5%	6-10%	11-15%	16-20%	21-30%	31%+
Price	56.5%	15.2%	5.4%	2.2%	7.6%	13.0%
Quantity	67.4%	13.0%	7.6%	3.3%	6.5%	2.2%
Wrong item shipped	60.9%	23.9%	7.6%	5.4%	2.2%	0.0%
Item was backordered	51.1%	25.0%	14.1%	4.3%	2.2%	3.3%
Bad item # / product description	77.2%	12.0%	4.3%	3.3%	2.2%	1.1%

A National Chain Advantage?

National distributor survey respondents said they typically get paid in 33 days whereas independent distributors responded within 45-75 days. The only possible explanations are either business mix (industrial accounts typically pay faster), credit collection practices, or the ability to offer e-invoicing solutions.

The research revealed that national distributors are more likely to send invoices via email, EDI or posting them to a secure website. Upon follow-up, it was determined that many of these distributors had agreed to contracted pricing for specific timeframes that could be adjusted based upon accepted indices. These practices will continue to expand throughout the industry as more distributors turn to third party expertise (Billing Service Providers) to support the execution of these value added programs.

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So, What to Do

To achieve parity, and reduce collection time, distributors and their customers need to plug into each other. A key step is for distributors to better understand their customers.

Our research revealed that unfortunately, not many distributors have surveyed their customers regarding their accounting systems or “e-invoicing” desires. Less than a quarter of distributors have surveyed their customers regarding their electronic capabilities.

Have you surveyed your customers regarding their e-capabilities & desires?	
Yes	23%
No	77%

The good news is that more distributors believe that their customers are beginning to understand the “total cost of their distributor relationships.” Among the distributor respondents, 26% believe that up to 50% of their customer base understands broader business issues.

What % of your customers do you perceive understand the concept of "total cost of relationship (ownership)"?	% of dist in 2006	% of dist in 2007
0%	0.0%	4.3%
1-10%	29.0%	21.7%
11-25%	51.6%	30.4%
26-50%	19.4%	26.1%
51-75%	0.0%	4.3%
76%+	0.0%	13.0%

As both distributors and customers recognize the need to tackle broader business issues we expect to see innovative cost-saving solutions, like electronic billing, become more prevalent.

Even in 2005, customers wanted distributors to offer web features like the ability to download invoices. In a survey we conducted then, 28.6% of customers responded that they knew a distributor who offered the “ability to download invoices” and 82.1% felt distributors should offer this service.

Further supporting the case for electronic invoicing, almost 40% of respondents surveyed in our 2007 study would like to receive invoices by email, almost as many as said by mail.

How would you LIKE to receive invoices? (Check all that apply)	% Response
Mail us a paper invoice/statement once a month	43.0%
Email to us as an attachment and we print them out	39.8%
Mail paper invoices to us as we pick up material	39.8%
Send invoices to us in an electronic file so we can print out	21.5%
Send invoices electronically via email or go to a website to directly import into our accounting package	19.4%
Distributor faxes invoices to us	19.4%
EDI invoices to us to import into our file	7.5%
Let us go to their website to download and print	5.4%
Salesman drops invoices off at our place of business	3.2%
Distributor/supplier posts invoices on their website	2.2%

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Distributors currently offering e-invoicing reported that 12 to 26% of their customers are receiving invoices electronically. Billtrust, a leading billing service provider, reports that they have many distributors who are delivering over 40% of their invoices electronically.

The survey also asked customers what they saw as the benefits of electronic invoicing. Over half identified *"receiving invoices faster"* as the key benefit. Other benefits included *"matching of P.O.'s to invoices"* and *"reduced time spent on accounting"*.

What, if any, benefits do you perceive by receiving invoices electronically? (Check all that apply)	Response %
Receive invoices faster from distributor so can bill customers faster	55.4%
Reduced time in matching P.O.s to invoices	47.8%
Reduced time spent on accounting	40.2%
Reduced time in posting invoices to jobs	35.9%
Easier to work with distributor sending information electronically	25.0%
Greater accuracy from my distributor	15.2%

It is reasonable to expect that distribution of paper invoices will decline as electronic invoicing rises. This improves customer satisfaction and reduces distributor costs. Additionally, distributors who are seeking to be more "green-friendly" can tout the fact that they will be utilizing less paper and reducing their carbon footprint.

So what to do? The data indicates that distributors will begin to offer an expanded set of invoice delivery solutions to their customers. The primary reason will not just be driven by the cost saving opportunities for the distributor but also by the simple fact that their customers "WANT IT."



Complete Billing Services Providers

Associations and marketing groups such as NAED, HARDI, IMARK Group, and Wit are encouraging their distributors to consider alternative invoicing methods due to increased costs. The ultimate goal is to help distributors improve profitability by reducing operational expenses, improve productivity and further differentiate themselves.

To that end they are endorsing service providers who can review and enhance a distributor's billing practices. These companies are generally called Billing Service Providers (BSP)

Billing Service Providers can provide many services to distributors including:

1. Evaluation of current processes
2. Return on investment analyses of potential billing systems
3. Evaluation of credit approval processes and terms
4. Handling of receivables internally within the company and with the customer
5. Bill delivery services via paper and electronic methods
6. Bill design services
7. Web based electronic payment services
8. Proof of delivery

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9. EDI for the distributor to their customer
10. Electronic files (e-billing) that import into a customer's accounting package.

The economy of scale that a BSP can offer is based on looking at centralizing and organizing security driven processes that can offer significant cost benefits to a distributor. Distributors who elect to outsource and automate their invoicing process report an approximate 32% cost reduction (based on an Institute of Management Administration, www.ioma.com, report). This savings is typically realized over a 45+ day period of time, and can be increased based upon the emphasis placed on adopting e-invoicing methods.

According to Michael Sugirin, Deutsche Bank, quoted in a Business Management magazine article (www.busmanagement.com), "Aside from cost savings, distributors may realize a reduction in their DSO's of 6-17 days." Our industry research revealed that distributors are realizing a 1-5 day improvement. Regardless of the number of days, distributors would welcome any addition to their cash flow through quicker collections.

Conclusions

As gross margins continue to contract, distributors will seek alternative processes to reduce operational expenses while improving their productivity. Through this innovative thought process, companies are able to "turn paper into profit."

Traditionally, accounting departments have been viewed as cost-centers. The advent of e-invoicing capabilities is breaking this myth. By reducing identifiable costs and improving collections, accounting can become a profit center (or at least less of a profit drain), adding value to an organization.

As technology has improved and companies are more willing to engage technology for confidential information, e-invoicing will continue to grow and change the invoicing landscape for progressive distributors and their customers.

About Allen Ray Associates

Allen Ray is principal of Allen Ray Associates, www.allenray.com. Allen Ray Associates helps companies improve profitability by proactively identifying changing market trends and issues. Executive briefings or in depth research helps a client to receive fresh and objective analyses. Allen can be reached at 817.704.0068 or allen@allenray.com.

About Channel Marketing Group

David Gordon is principal of Channel Marketing Group, www.channelmkt.com. Channel Marketing Group provides market research, marketing plan development and strategic planning resources for manufacturers and distributors. He can be reached at 919.488.8635 or dgordon@channelmkt.com.

About Billtrust

Billtrust™ is dedicated to improving the billing process for distributors, saving them time and money. The company has developed state of the art products and services designed to simplify bill delivery and payment.

Billtrust offers a suite of outsourced billing solutions, called CompleteBilling™. This comprehensive solution includes outsourced paper billing, fax billing, email billing, hosted online billing and payment (EBPP & EIPP) and a web-based bill archiving and customer service tool called CustomerCare.

Visit www.billtrust.com or call 888-580-2455 for more information.

