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Your Guide to Direct
Debit: **Best Practices to
Maximise Cash Flow**

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Executive Summary

When you take recurring or subscription payments, each customer represents significant long-term potential value to your business. That's why it is so important to exceed customer expectations and deliver an unforgettable customer experience.

With evolving customer demands and volatile markets, how do you know you have chosen the right Direct Debit solution for your business? How often do you evaluate what is available and how your competitors are using these services to gain an advantage?

The objective of this eBook is to provide clarity on the latest innovations in collecting recurring payments via Direct Debit so you can make the right choices for your business.

Even if you already have a long-term solution in place, this guide will share best practices and thought-provoking ideas to further streamline processes and enhance the customer experience.

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Direct Debit is Here to Stay

The payments landscape has gone through significant transformation in recent years. Technological advancements have led to growth in innovation, with payments becoming faster, easier, and more convenient.

The subscription economy continues to expand, with many SMEs now participating. New variable recurring payments (VRP's) offer a method of payment that could combine the low cost of Direct Debit, with the speed and flexibility of cards, which could be a powerful alternative for this growing market.

Looking back, a much earlier innovation in payments came in the 1970s with the arrival of Direct Debit itself. For several decades, Direct Debit became the most popular method of collecting bank-to-bank transfers in the UK.

Today, almost 50 years on nine out of ten British adults make a regular payment via Direct Debit, and three out of four household bills are paid in this way.

Direct Debit is one of the safest payment options for customers and is cheap for financial institutions and billers to run. Most new innovative payment methods are underpinned by card payments or Faster Payments via Open Banking, but the latter have no indemnity if things go wrong, hence why most organisations partner with a business payment expert to ensure a smooth process.

"In 2020 there were **4.5 billion payments made by Direct Debit**, a rise of 1% over the previous year, with an overall value of £1,178 billion". *UK Finance – 'UK Payment Markets 2021'*

For businesses, Direct Debit provides increased cash visibility and control, reduced risk, and the opportunity to streamline processes. For customers, Direct Debit doesn't incur transaction fees for the payer, it minimises administration, enables payments to be spread, and provides a money-back guarantee in the event of an error.

Direct Debit is a clear winner in the payments landscape, but how do organisations ensure they are getting the most from their current setup and service providers?

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The Role of the Service User Number (SUN)

A common misconception in the industry is that Direct Debit should only be used by large corporations. Historically, this used to be the case, as only bigger and more established businesses could obtain the required sponsorship from their bank.

However, as payments evolved, third-party organisations are now permitted to organize and collect Direct Debits on a customer's behalf without a bank getting involved. This enables smaller businesses to outsource some of the risk associated with processing Direct Debit's themselves.

SO, HOW EASY IS IT TO SET UP A DIRECT DEBIT?

A Service User Number (SUN) is a unique six-digit code given to each organisation that collects money via Direct Debit. You can't introduce Direct Debit to your business without one and it acts to identify each company signed up to the scheme.

Should I apply for a SUN?

Bacs is the organisation that processes all Direct Debits and manages the SUN database. It uses the SUN in all its communications including each corresponding transaction record. In the case of Direct Debits, the SUN represents the Service User, essentially the organisation collecting or receiving the payment.

Unfortunately for smaller businesses, Bacs will only issue a SUN to organisations sponsored by the UK's major banks. If your organisation can meet certain criteria based on size, expertise, and indemnity, it's a good idea to acquire a SUN.

Direct Debit Management experts such as Bottomline, can help ensure you deliver a consistent user experience across all payment channels.

All is not lost if this isn't the right option for you. Perhaps you are a small business that wants to take some of the risks out of the Direct Debit process? In this case, a third party can do all the hard work for you, managing and submitting payments to Bacs while you concentrate on other areas of the business.

The third-party option eliminates the responsibility of having to meet the bank's strict criteria. Instead, it's the third-party or bureau that must satisfy Bacs' requirements throughout the transaction.

In short, this means you don't have to worry about the complex Bacs Direct Debit Scheme rules and prohibitive practices that exist – leaving you to focus on other priorities.

Many businesses select this affordable option as it is ideal for those starting their Direct Debit journey. It is well suited to sports clubs and charities to big utilities that need to take reoccurring payments such as a monthly subscription. It's also useful for businesses that have ongoing relationships with customers where regular invoicing is required.

Direct Debit Management experts such as Bottomline, can help ensure you deliver a consistent user experience across all payment channels. This can include creating a branded web page either hosted by the provider or you will be given the option to use an API for your customers to sign-up to online.

There are many different providers and offerings out there that claim to make the Direct Debit process more efficient for those that have procured a SUN, but how do you determine the right options for your business? It might be that you are attached to your current service provider because it's what you've always done, and you are apprehensive about change.

Many of the options below enable improvements to be made by leveraging technology and automation. Can these options further reduce Days Sales Outstanding (DSO) and the cost to acquire new customers? It is important to evaluate your current investment at each stage of the Direct Debit lifecycle and look at best practices for optimisation.

Streamlined electronic processes reduce failure rates and improve the time to the first collection.

MANDATE CAPTURE

Before you can collect payment by Direct Debit, your customer must issue you with a mandate. This mandate is called a "Direct Debit Instruction", or DDI, although it is commonly referred to as a "Direct Debit Mandate".

Paper Versus Paperless

A Direct Debit Instruction is an authorization from your customer to collect future payments and these can be collected on paper or electronically.

Any organisation embarking upon Direct Debit for the first time must use the electronic Bacs service – AUDDIS. However, many organisations still choose to do this manually which presents several challenges to the customer and vendor.

Paper DDIs can be suited to businesses that meet customers face-to-face, as they can be completed on the spot directly with the customer. Customers don't need to be online, so this is often more suited to the elderly. However, this option does still involve printing, postage, and storage which can lengthen set-up time and incur higher costs.

Paperless Direct Debits do not involve filling in a paper Direct Debit Instruction. Instead, the authority to debit a Payer's bank account is collected either on a website or over the phone and the Direct Debit

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"As many as 70% of organisations are still undertaking Direct Debit manually, **risking delay, payment error and additional costs with Bacs estimating that every Direct Debit failure costs £50 to repair**".

Pay.UK Research

Instruction is sent to the bank electronically via AUDDIS. Within days, a notification needs to be sent to the customer confirming the details of the DDI. The payer also must be notified as to when collections will be made.

Streamlined electronic processes reduce failure rates and improve the time to the first collection.

Any failures in setting up authorization from new payers are communicated via Bacs reports. By leveraging paperless Direct Debits and AUDDIS, the risk of transposing details incorrectly is significantly reduced since the Instruction is submitted automatically to the payer's bank or Payment Service Provider (PSP).

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Account Validation

AUDDIS service users must undertake validation checks to validate the payer and the account details before processing any Direct Debits. Failure to do so may lead to unauthorised/fraudulent DDIs being set up resulting in Direct Debit indemnity claims being raised.

To maximise the effectiveness of the DD process and minimize DD failure, account validation and verification is the recommended best practice. These processes can significantly improve your straight-through processing rates and deliver improved customer service, simply by confirming your customer's account details in real-time.

THE VALIDATION PROCESS:

• Checks that a bank account and sort code are valid

• Ensures a specific bank account number fits the rules that associate it with a specific sort code

This enables 75% account validation but how do organisations manage those accounts without a credit history? Specialist providers such as Bottomline allow businesses to scan a photo of a passport or driving license to provide another key KYC validation check.

ACCOUNT VALIDATION AND VERIFICATION

"71% of Direct Debit failures are due to bank account and sort code error".

Bottomline Technologies – The Hidden Cost of Direct Debit & Direct Credit Research, 2013

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Account Verification

For organizations planning to be paperless, the verification process is mandatory and involves matching bank account and sort code to personal details to confirm the account exists.

This process reduces the likelihood of fraudulent DDI's being set up and collections being taken from an account that doesn't belong to the right person. Ensuring these checks are in place will reduce the likelihood of illegitimate refunds being performed under the Direct Debit Guarantee.

Organisations managing this independently would need to ask the payer to provide a bank statement to prove ownership of the account, which is time-consuming and prohibitive, versus leveraging an automated solution that can manage this process for you.

"**£456m was lost to APP fraud in 2019 with only 25% of the funds recovered**".

UKFinance.org.uk

With payment fraud on the rise, organizations are introducing additional checks to reduce incidents of Authorised Push Payment (APP) fraud where fraudsters trick customers into sending a payment to a bank account in their control.

Confirmation of Payee (CoP) acts as an account name checking service that provides payers with the assurance that payments are being sent to the correct company/person. Working with a payment specialist such as Bottomline, this can be easily switched on leveraging your existing Direct Debit Management solution.

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6 Scheme Management

Scheme management is the process of managing who to take payments from and when. Surprisingly, 30% of organisations manage this process using Excel. Other tools include an in-house built solution or a fully-fledged Direct Debit Management solution.

If most of these processes are currently managed manually or by leveraging an in-house solution or contract management tool, you could be in breach of Bacs rules. It could, also be impacting on the efficiency of your operations.

A Direct Debit Management solution manages the entire Direct Debit lifecycle, enabling organisations to tackle the issue of failed payments early on, with the use of recurring payment intelligence tools. This empowers businesses to be more efficient by reducing the admin burden and time to get paid.

TO EVALUATE THE RIGHT OPTION FOR YOUR BUSINESS, IT'S IMPORTANT TO CONSIDER THE FOLLOWING:

- **Are you storing your payers and bank account information securely? Are you meeting Direct Debit scheme rules for security?**

- **Are you able to make accurate cash flow forecasts and review Direct Debit performance?**

- **Do you have to use a different system for one-off and regular payments – how do these feed into the reporting processes?**

- **How much time do you spend calculating amounts and collection dates for your customers?**

- **How do you access, review and act on the messages that Bacs make available to service user numbers to help with Direct Debit Processing?**

- **How do you keep payers informed in line with scheme rules?**

- **What is your process for preventing and defending unwarranted indemnity claims?**

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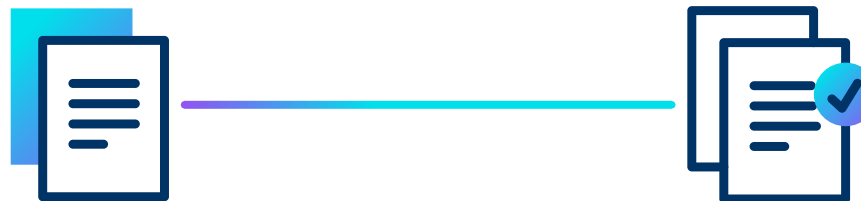
File Submission

This is the point at which you can lodge the Direct Debit mandate and submit the relevant forms for payment to be made.

Most organisations do this by leveraging Bacstel-IP (BACS) or a Bacs bureau. Organisations submit Direct Debits due for collection from their back-office system and generate an input file which is submitted to the Bacs service for processing.

There are strict Bacs rules that organisations must adhere to, for example, the file must be submitted at least 2 working days before the Direct Debit due date. Direct Debits must be sent to the payer's sort code and account number and each Direct Debit record must be submitted with the appropriate transaction code.

This complexity and number of rules explain why over half of the organisations using Bacs services in the UK make their Direct Debit and Direct Credit payment submissions through a Bacs Approved Bureau, rather than submitting files directly to Bacs themselves. The bureau will generate and submit the file in time for the Direct Debit collection due date(s) and ensure any rules are adhered to.

If your organisation has or can gain approval to operate your Service User Number, you can use a Bacs Bureau to submit your payment and make your collections. This means you retain the relationship with the payer, giving you the flexibility to change providers further down the line.

Alternatively, you may choose to leverage Bacstel-IP, a secure access channel for submitting Direct Debit payments and Direct Credit payments directly into the Bacs system in the UK (direct submitter). You'll also need Bacs-approved software to submit payments using this method.

An organization can also develop their software which can submit files of payers and their payments to Bacs in a predefined format (known as Bacs 18) or partner with an organisation that can manage this process on their behalf (indirect submitter).

Direct Debit Management experts such as Bottomline can advise which option will support you best.

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LET'S LOOK AT THE KEY FEATURES OF EACH:

	Direct Submitter	**Indirect Submitter**	**Third-Party Managed Service**
Who Submits:	YOUR ORGANISATION	BACS APPROVED BUREAU	BACS ACCREDITED FACILITIES MANAGEMENT (FM) PROVIDER
Key Features:	• Your organisation will need to be sponsored to use Direct Debit by a Bacs participant PSP (such as Bottomline) • Your organisation is likely to undertake all of the key activities involved, from getting authority from payers, maintaining the required records, preparing files of payments to be collected, and submitting them directly to the Bacs Payment System	• Your organisation will need to be sponsored to use Direct Debit by a Bacs participant PSP • At least the final part of the process (the submission of the files to the Bacs Payment System), is undertaken on behalf of your organisation by a third-party - a PSP or a commercial bureau • The level of the activities undertaken on behalf of an organisation by a bureau can vary and will be subject to individual contractual agreements between you and the bureau	• An FM provider is an organisation with responsibility for all aspects of the Direct Debit process and will forward collected funds to you (known as the FM client

Source: Little Bacs Guide to Becoming a User of The Direct Debit Service

This most appropriate for your organisation is likely to be driven by the volume of transactions involved and the level of sophistication of processes you wish to use. Direct Debit Management experts such as Bottomline can advise which option will support you best.

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CONCLUSION:

Making the Right Choices for Digitalization

Direct Debits are a familiar and widely trusted method for paying regular bills, but the goal should always be about maximizing cash flow and making sure in simple terms, you just get paid, on time and in full, as often as possible.

There are several options to consider at each stage of the Direct Debit process. The solutions you choose will depend on several factors such as the number of customers you are servicing, the volume of payments processed each month, and the value of payments.

Some providers for example will impose limits on the collection dates, the number of collection runs per month and the amounts collected. Without this flexibility, you may find future business opportunities restricted.

In addition, you should consider the largest amounts that you will typically collect from your customers and confirm that your provider can accommodate this. Some providers will limit you to £5,000 per transaction, which could rule out some of your customers from signing up to Direct Debits in the first place.

As a small business processing reoccurring payments each month, using a Direct Debit provider who can sponsor you onto the Bacs Direct Debit Scheme makes a lot of sense.

A fully branded solution helps you to deliver a consistent user experience for your customers across all payment channels. You should also evaluate how and where do your customers like to buy? Ideally, you want to be able to offer a consistent customer experience across multiple channels – online, mobile, offline, and in person.

In our view, businesses must embrace digitalisation and automation if they want to increase cash flow, reduce days of sales outstanding (DSO) and the cost of customer acquisition. As collection volumes grow, the management of these transactions will only become more complex, error-prone, and time-consuming if they are managed manually, or with software that is not fit for its purpose.

Chasing debt, late payments, and managing the complexities around Direct Debits can be made much easier, whether you choose to implement one platform to manage the entire Direct Debit lifecycle or individual solutions that can improve efficiency and increase cash flow. It's all about ensuring you have the best solutions and practices in place for your business to be compliant and just get paid.

"Bottomline Technologies has enabled us to eliminate the complexity of managing Direct Debits and move towards a paperless operation. We have improved efficiency across the Direct Debit lifecycle whilst ensuring full compliance with Bacs Direct Debit scheme rules"

The British Academy of Cosmetic Dentistry

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