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**Management Report**  
by the outsourcing  
consultants at Smyyth LC

## **Deductions Management Systems ROI Accounts Receivable, Deduction and Dispute Management Practices**

*Smyyth is an accounts receivable, collection and deduction management outsourcing and technology firm with decades of experience working with great companies to solve revenue dilution and profit losses due to deductions.*

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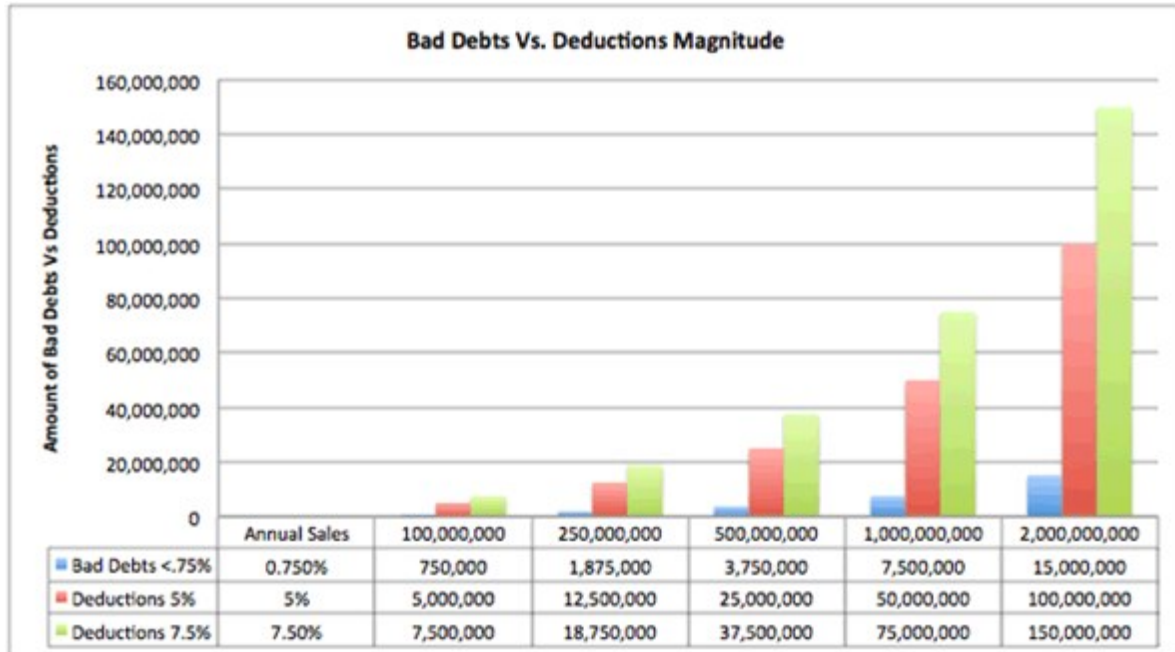
Great deduction management software designed by expert practitioners will produce an impressive ROI through quicker and more accurate deduction and dispute resolution, reduced revenue dilution, improved profit recoveries, better accounting controls, Sarbanes-Oxley compliance, and all with much lower labor costs.

Why should you care about this arcane problem?

1. Disputes and deductions (depending on the industry) represent huge profit losses and revenue dilution for many companies -- 5 to 10 times the amount of bad debts.
2. Excessive deductions are indicative of operating, processing, and billing snafus in your company that you need to fix.
3. Large amounts of overhead and labor are spent on this administrative function.
4. Customer dissatisfaction with your inability to get control over the issues causing deductions will hurt your business and your "supplier scorecard" rating.

## Bad Debts Vs. Deductions - An Example of the Costs

This chart will give you an idea of the relative importance of deductions to bad debts in a typical case.



As you see above, even for a small to mid market company, the amount of annual deductions expenses is a very big number, one worthy of serious top level attention and investment to get under control.

## Deduction Categories and Costs

**Agreed to Business Practices**, such as Trade Promotions, Discounts, Markdowns, Approved Returns. This category represents the largest percentage of deductions taken although they still have a very high error rate (customer applied wrong price, deducted for too many units, etc.)

**Preventable Deductions - Process Errors**, such as trade promotions not explained clearly, supplier pricing, billing, EDI, packing and shipping errors, where the shipment and invoice does not match the order specifications. These are often systemic, and will

continue costing money forever unless the root cause is identified and solved.

**Unauthorized or Excessive**, such as trade promotions not executed according to the deal parameters, late discounts, or customer returns errors, pricing, receiving counting errors. Excessive amounts deducted on otherwise proper deductions are included here as well, including too-high returns pricing, incorrect quantities charged back, etc.

Perhaps 80% of deduction dollars are correct; however, our experience is that the majority of deduction documents - even those that are part of “Agreed to” category - contain errors -some small, some large -that in the aggregate cost the creditor huge profits. Since the deduction volumes are often beyond effective manual handling, and most accounts receivable systems are good at bookkeeping but without resolution tools, it is essential to consider add-on software or expert services to solve this lost profits problem.

## **Deduction Management System Benefits**

If you select the right system, here are some of the important benefits you should see.

- **Deductions Prevention** — Active root-cause identification so you can prevent errors and disputes upstream in the order cycle that will eliminate systemic, preventable deductions.
- **Automated Deduction Management** — Categorize, assign ownership, escalate, and track deductions to resolution using workflow that enables cross-departmental collaboration.
- **Deduction - Credit Memo Resolution** — Automated research tools for reconciling deductions vs. credit memo data, even down to the SKU (line item) level so you can reconcile returns variances with one click instead of a spreadsheet and hours of work.
- **Real-Time Reporting and Analytics** — Analysis as to the causes of deductions, and use this new insight to drive continuous process improvements, and department staff performance monitoring and management.
- **Increased Recoveries - Collections** of excessive or incorrect deductions with proper documentation backup and workflow that manages the recovery process.

- **Increase in corporate profits and cash flow** through much better performance and reduced overhead.
- **Proper accounting and audit trails** that enable you to account for and justify deductions and trade promotions so you do not run afoul of Sarbanes-Oxley or FTC violations.
- **Substantial Overhead Reductions** — Lastly, with an automated system driven by management-directed workflows and escalations, along with the qualitative improvement in results, you will see significant reduction in the labor required for this function. You will be able to do more with fewer people.

## Selecting a Deduction Management System

Selecting a system can be confusing, so let's start with a set of basic specifications based on your own operational needs and experience and add to it as you review various systems and you see how others are using the software. You will soon develop a list of Must-Haves, Nice-to-Haves, and Not-That-Important features.

To begin, in this age it make no sense whatsoever to consider installing client-server software; that is, having an "in-house" system. The web is the way to go, with a "Software as a Solution" (SaaS) system. No software, no hardware to purchase or install - just your web browser and you are ready to go from anywhere, plus a data linkage with your other financial systems. This way, outside sales people, business partners, and even customers can have easy access to the same information to collaborate or participate in problem solving and accounts receivable management.

The deduction management system has to be "intuitive", that is, easy to understand and navigate, so workers can become power users. Your challenge will be to find a combination of capability and streamlined simplicity in one package (look at of Carixa <sup>TM</sup> to see how this is accomplished). Deduction-management software that is complicated, has too many windows, or requires offline work for end-to-end job completion will cease to be used effectively as personnel turn over. A deduction-management system needs to be intuitive so a normal user can pick it up with one day's training.

## **Accounts Receivable Deduction Management Features**

Accounts receivable management is rife with functions that are only partially automated, still manual, or which need to be done offline, for example, by using Excel. The right system will encompass all of these and will automate, at a minimum, these features and eliminate offline processes:

- EDI capabilities from 810 invoice processing to 820 cash remittance
- Auto match with character string matching against multiple fields
- Automatic deduction - chargeback creation and workflow routing for action and approvals
- Splitting deductions amongst expense categories and / or credit memos
- Acquisition of proofs of deliveries and debit memo documents from carriers and customer systems
- Mapping your system to customer codes to eliminate unidentified deductions

**Workflow and Scheduling Actions** need powerful rules engines so that the right people handle deductions at the right time, with nothing slipping through the cracks. Profit leakage because receivables slipped through the cracks can be eliminated. It goes without saying that your system needs both account and transaction-level default and user-specified follow-up dates, but it also needs to be able to escalate important issues to upper management by customer, dollar amount, or age, the criteria management determines in setup. Using pre-set rules on allowable resolution times, the system should generate a follow-up with the right person, as well as escalating the issue at the right time.

- Customizable workflows at the customer and detail level with a built-in escalation
- Prioritizing actions based on user-definable criteria
- Customer A's freight deductions go to Joe in traffic
- Customer B's trade-promotion issues go to your sales manager or broker.
- Approvals for write-offs or adjustments would be routed to management for approval.

**Contacts, Communications, and Actions.** The system should expedite internal and external communication, collection, and resolution. Check to see that it will automatically communicate by fax, email, letter, etc.

- Enable mass communication to a group of customers by email, letter, or fax, say for a terms reminder or address change.
- Automatic transmission of chargebacks and collection letters
- “One-click” placement with collection and outsourcing firms

**Customizable Management Reporting and Dashboards.** You need hierarchical views and reporting from the CEO level, to sales, to the manager, and analyst to provide a quick performance overview, with drill-down capability. Extensive deduction coding and analysis to provide root-cause feedback to nip systemic problems in the bud.

**Audit Controls.** With all the Sarbanes-Oxley issues concerning trade promotion and pricing allowances, you need to track how deductions are resolved and accounted. Trade payments accounting is especially important. What is needed is the ability to view the history of past applications and offsets.

**Communication with Other Systems.** Lastly, the easiest way is to transfer data with your AR application by scheduled upload/download (by the hour, day, etc.). The perception that “real-time”, second-by-second updating with AR data is needed is almost always bogus. This type of integration is very expensive to accomplish and almost always unnecessary.

## Summary

With the right dispute and deduction software, you will (i) save significant overhead expense while (ii) reducing future deductions by solving root causes, (iii) improving deduction days outstanding (DDO), and (iv) being able to recapture - collect much higher

percentages of erroneous deductions. All in all, you should recoup your investment in the first year if you choose the right solution - a return on investment that would impress the most jaded CFO.

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