



LENIC CONSULTING AND TECHNOLOGY SERVICES LIMITED

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(Formerly CCJL Services Group Limited)

The Truncation Roadmap

What is truncation?

The terms “truncation” and “Check 21” have been debated throughout the global financial community since 2004. Many different interpretations exist but, at its core, **truncation** is the process by which the physical movement of cheques within a bank, between banks or between banks and the ACH is eliminated (in part or in full) and the cheques are replaced by electronic records of their content, with or without the images. The electronic records are then used in much the same manner as the physical cheques. **Check 21** is simply the name given to the US truncation initiative. A bank may truncate any or all of the four areas of cheque processing, namely in-clearing or out-clearing of cheques and/or returns.

How does truncation help me?

From a service delivery perspective, the main benefit of truncation is that it streamlines the cheque handling process and gives customers quicker access to their cash. However, for the banks that choose to go this route, there are a wide range of additional benefits, as follows:

- ✓ faster clearing and settlement process allowing for a reduced float;
- ✓ reduced cheque handling overheads;
- ✓ increased operational efficiencies;
- ✓ improved information security through reduced cheque losses in transit;
- ✓ new revenue opportunities through add-on services.

Do I have to truncate?

While cheque truncation is seen as the next logical step in payments processing, it is not mandatory...now. But, given the considerable financial savings and efficiencies that result from truncation, those that at first decide not to truncate may find themselves dragged into the truncation initiative through the application of exorbitant fees for the cheques that the post-truncation banks must process on behalf of the pre-truncation banks. And, as more and more banks implement truncation, they will likely lobby regulators to mandate that that the remaining banks come on board. It is therefore more prudent for institutions to prepare for and implement truncation on their own timetables instead of being mandated to do so by external entities.

Can I truncate now?

While there are many issues to consider prior to truncation, there are three critical areas that absolutely must be addressed and the systems put in place before a bank can begin to consider embarking on a truncation initiative.

1. *Remote Image Capture* – There must be a system in place to capture the cheque images and MICR data and this system must be decentralized from the actual processing of the physical cheques.
2. *Electronic Cheque Presentation* – Since the bank will no longer be returning the physical cheques to their customers with their statements, there has to be a system in place that allows their clients to easily view the images of their cheques. This can be facilitated through the use of electronic statements delivered to the client either via email or as a service on the bank’s online banking platform.
3. *Cheque Image Security* – The security provided by the armed couriers during transportation of the physical cheques must be replaced by information security measures of at least an equivalent level during the electronic transmission of cheque images to the final processing/storage site. Data integrity protection tools such as encryption and digital signatures are often used.

It is important to note that what is not mentioned here is the passing of any truncation-related legislation. While it helps to have the appropriate e-friendly legislation in place to support the validity of electronic images, the absence of such does not have to be a deterrent to truncation since the physical records can still be stored for the requisite period and accessed only if required.

How do I prepare for truncation?

Once the major impediments are removed, there are other questions that must be asked and answered before proceeding with a truncation initiative. Some of these are listed below.

- ✓ Are we going to allow customers to opt in/out of truncation?
- ✓ When should we capture the cheque image? Before or after encoding?
- ✓ Do we want any ex-branch capture points i.e. ATMs, mobile and home deposits?
- ✓ Do we truncate at the branch or the teller level?
- ✓ Is In-house or outsourced processing of the physical items the best route for us?
- ✓ What is the best image format to use and do we have enough bandwidth for image transfer?
- ✓ Which physical items will we retain and where?
- ✓ What investments must we make in new systems, modifications to the core banking application and process re-design?
- ✓ Should we consider cheque format standardization?

- ✓ Do we want to employ image replacement documents (IRDs) in case we want to destroy the cheques later?
- ✓ Is my information security framework capable of handling the new risks associated with truncation?
- ✓ How do I sensitize my customers and obtain buy-in to the truncation initiative?

How can LeNic help me?

While a bank may prefer to take a particular route towards truncation, depending on its own internal business strategies, there really is a “best” path that will take the institution where it needs to go with the least amount of organizational upheaval and lowest incremental spend, while allowing it to still remain competitive and agile. To that end, we have created the *LeNic Truncation Roadmap* that leverages our own 25 years of experience supporting IPoD environments as well as the combined experience of business partners who are considered to be global leaders in the field of payments processing.

LeNic has chosen to offer its truncation roadmap at this time because, even though there is no overt pressure being exerted by local and regional regulatory bodies, based on current trends, we believe the following to be true.

- ✓ Industry support for a centralized processing environment will decrease as the truncation initiative approaches maturity.
- ✓ The Caribbean will not be able to put off truncation for much longer if they want to continue to be competitive in the market.
- ✓ The banks that can make the shift to truncation quickly and seamlessly will be the ones that will stand to realize the greatest benefits from client migration.

The roadmap is designed to be effective regardless of where you may be on the journey to truncation. So, whether you’re almost ready to flip the switch or remote image capture is still a proposal on a desk, you will be able to align any future investments in this area to a structured transition plan with a specific intended outcome.

The Road to Truncation

At the core of the LeNic Truncation Roadmap is the flexibility and modularity of Aperta’s AiDPS platform, which allows our clients to add new functionality to their IPoD environments as needed, all while leveraging the powerful information asset that is their existing cheque image archive. The roadmap consists of 8 major phases, executed over a period of 3 to 5 years:

#1 Stop investing in technology that will perpetuate the current status quo. – What this really means is “Don’t buy anything that you cannot take with you into truncation.” Manufacturer focus is shifting to truncation technology, therefore why invest in technology that may very well soon become obsolete? If additional equipment is required to create redundancy or as a contingency, it can be leased from LeNic until centralized operations are either outsourced or eliminated entirely.

#2 Implement Remote Image Capture. – For banks that do not already employ remote capture, this step is required

to separate the truncation-related operations from those other activities that are not necessarily required in a post-truncation environment. Both Aperta’s *Branch Capture* and *Teller Capture* modules will allow banks to make the transition while still leveraging their AiDPS image archive.

#3 Implement electronic statements. – Aperta’s *Ai Statements* module uses the cheque images and data captured at the branch back-office or tellers to create image-enhanced e-statements that can be delivered through a variety of channels, including CD, email and online banking. For the clients that choose to participate in this service, there will no longer be a need to physically process their cheques. Therefore truncation by account will have been automatically achieved. Additionally, strategic selection of the first recipients of the e-statement service can net significant savings for the bank.

#4 Perform an iSecurity audit. – Using its distinctive *Target-Aligned Security Framework (TASF)* methodology, LeNic will conduct an audit of the bank’s information security infrastructure to ensure that it is robust enough to support the shift from paper-based to fully electronic payments processing.

#5 Reduce the overall volume of physical items to be processed. – This is accomplished through the use of online character recognition (OCR) technology, which reduces the number of items that must pass through the data correction and balancing (DCB) process. Burroughs’ *SoftCAR+* can reduce the volume of cheques passing through the DCB process by as much as 75% when used in conjunction with the proper cheque design.

#6 Reduce the volume of “on-us” physical items to be processed. – This refers not only to increasing the number of payment channels but also to the introduction of more avenues for image cheque presentation. Aperta’s core AiDPS application is highly customizable and can be configured to capture images from a variety of alternate channels, including ABMs and smartphones.

#7 Outsource remaining centralized cheque processing functions. – The central sorting centre requires the largest capital expenditure and attracts the majority of externally-driven overheads. By “operationalizing” this function, the bank is free to redirect spend to other areas. Also, the cheque volume has now been reduced to a level that will ensure the lowest possible fees paid to the outsourcer. LeNic’s outsourcing service offers savings to the client of up to 85%.

#8 Full truncation. – The bank is now in a position to decide if it wants to go forward with its truncation initiative and truncate for all clients or whether it will allow some clients to continue to use cheques. However, at this stage the cost of processing the paper cheques has been reduced to its lowest point through the previous initiatives, so the decision can be based more on customer service and not on necessity.

Service like no other

LeNic continues to be committed to providing superlative technology services to our clients and we stand ready to assist wherever and whenever our products, knowledge and experience can be of value.