

Implications of the Electronic Funds Transfer System for Non-Financial Corporations

Richard F. Dundore

This symposium has been assembled at what I think is a most opportune time. It is probably more necessary this year than in any previous year of the developing electronic funds transfer system. In previous meetings of this nature, participants have tended to concentrate on the character and dimensions of the transfer system that would be required. At this time, interested institutions and groups appear to have pretty much jelled their thinking and to have developed their particular thrusts for dealing with the funds transfer system; and, in fact, many have found their preferred approaches.

In the process I sense we have reached a point where emerging competition is dominating the thinking of participants more than the spirit of open inquiry and mutual assistance that one time seemed to characterize our discussions. We started out with an effort to smooth the flow of dollars and control the rising flood of paper before we are drowned in check processing. We have now gravitated into what looks like a race for who will capture the most consumer participants and their household accounts.

Under the circumstances, we want to thank the Federal Reserve Bank of Boston for inviting us to present our views on the Electronic Funds Transfer System and its implications for corporations — that is to say, for non-financial corporations. Although personally I am a banker by profession, it has been my pleasure to serve for the past several years as head of the research group within the Credit Research Foundation that has dealt with the emerging problems of automation of the payment system for the business community. The Research Foundation, whose membership is made up of representatives from 500 major corporations in the United States, serves as the principal education and research arm of the credit fraternity. I am pleased to have Dr. George Christie, Research Director of the Foundation, in attendance at this symposium with me.

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*EFTS Planning Dominated by Consumer,
Not Business, Payments*

Our concern with the present stage of development of electronic funds mechanisms is primarily with their impact on the administration of business-to-business payments. But corporate financial policy must occupy itself also with problems of other parts of the emerging electronic system and must deal with the individual or non-business environment. Therefore, we are more than a little interested in the emphasis of most of this symposium on consumer payment procedures.

All too often it has been assumed from the magnitude of payments made by consumers for retail purchases and bill paying, that business firms will interface easily with the electronic mechanism once established. There should be little problem in extending its use to deal with business payments as well. However, the economic factors involved in controlling payments of individuals are multiplied many times over when dealing with corporate business payments. Therefore, let me spend the next few minutes as advocate for the interests of potential corporate participants in what we see as the inevitable emergence of a fully automated payment system.

First of all, we have been told that the volume of checks has been rising at a rate that could bring about a collapse in the collection system. The number of checks written in the United States has increased from 12 billion in 1960 to an estimated 27 billion in 1973. If this growth continues, there may be as many as 54 billion items by 1985. Yet, the handling techniques have improved steadily and the business community has been largely isolated from any ill-effects of temporary congestion. This is partly true, I think, because the hand labor of checks has tended to be spread out among countless banking units and corporate accounting centers.

Secondly, machine-handling of checks has improved remarkably during the same period and has offset rising clerical or administrative costs of processing. Needless to say, the value of deposit balances has also risen, so banks have not significantly changed their charges to business for such service. Again, by spreading activity among multiple banks, business has enjoyed an incremental cost situation. A \$10,000 check has never really cost more to process than a \$10 check. On the other hand, if we have reached the peak of this technology cycle, a change in this cost situation may be imminent; but it is not yet evident. Meanwhile, a considerable amount of effort is going into the reduction in transit rejects, and screening checks in bookkeeping.

One of the greatest insulators of cost has been the money value factor represented by the growth in Federal Reserve float, which has gone from an average \$1 billion in the 1950s to about \$3 billion currently. So far as I can understand, the change in Regulation J in late 1972 succeeded mainly in stabilizing this average float experience, and the Regional Check Processing Centers have helped hold the level under control despite rising check values. Fortunately for business, holiday delays, and transportation

or weather crisis problems have been largely filtered out by Fed payment schedules.

Therefore, the check has remained as a very well-established mechanism for business. It has most of the best attributes of a payment instrument: it is a well-documented evidence of payment; it can be converted to usable funds by recipients with a minimum of effort or delay. On the surface there appears little cause for urgency in espousing electronic funds transfer precepts.

Competition for Business Payments

Nevertheless, business administration is driven into the emerging electronic banking scene by the same problems as banks and similar prospects for more easily manageable operations. The real impetus, however, is coming from an area other than strictly cost savings. There is now a growing sense of competitive self-interest among financial service institutions, and we are only just beginning to see the tip of this iceberg.

Infighting has already developed between savings banks and commercial banks for free access to automated clearing houses; and between independent banks and the Federal Reserve for control of the message switching system; and between regional clearing houses and savings banks and their associations over separate or common national switches. Corporations, I think, are disposed now to sit back until the flack has cleared, before deciding where or how to direct their automation business.

Banks, for instance, may see the quantity and dollar volume of payments passing within their institutions, but they are ultimately more concerned with the useful deposit base and earnings potential of business payments. How important are business payments? According to the Bank Administration Institute's projections reflecting research data collected in 1967, about 18.7 percent of all checks written represented payments by business to other businesses. A study by Arthur D. Little, Inc. published in 1970 for the ABA Monetary and Payments System also estimated checks written on demand deposit accounts at 52 large banks in April, 1970. This study suggests that business-to-business checks represent about 39 percent of total check volume. For checks over \$500 this category accounts for about 61 percent of checks processed. From our studies in the Credit Research Foundation, each business-to-business check written represents payment on average of three transactions, and may represent thousands of invoiced transactions, so the payment problem become magnified.

The relationship between businesses and individuals is equally impressive in numbers, if not in average dollar value. Thirty-seven percent of all checks written were sent by individuals to businesses; and 26 percent from businesses to individuals. This is a basis for substantial business participation in EFTS, but the question is how and by what EFTS mechanisms.

Let us look at these numbers another way. BAI has estimated a third of all checks are drawn on the bank within which they are deposited, one-third travel less than 200 miles, and another third travel long distances. They tend to spend three business days on average within the banking system, i.e., from time of deposit to time of final presentation. I understand also that checks over \$10,000 are not generally sent through the Fed system, which means big checks have moved through the correspondent system. With the institution of Regional Clearing Centers, however, this is changing, both to reduce the number of days fractionally, and to fine sort and clear more checks by the RCPCs.

Viewed from a standpoint of deposit value, business checking activity normally generates substantial demand deposit balances. We estimate the deposit value is much greater in business-to-business payments than in any other business-related transactions. Payrolls clear locally and promptly; bill payments are mostly local and also clear promptly. But, we must add two days or more on average to reflect the mail experience of business payments. Hence, commercial accounts have a deposit structure with a built-in mail float and check presentation float equal to four or five business days on average. This represents a significant factor in the bank deposit structure, as we can readily surmise.

As an example, if we judge by the figures reported in the *Survey of Current Business* this year, manufacturing and trade sales totalled \$1,734 billion in 1973, or about \$6.9 billion per business day. Estimating five days of deposit float in the business payment system, this level of activity may well have accounted for upwards of \$35 billion of commercial deposits. This is almost equal to the average daily required reserves of all member banks. This pays for a substantial amount of check processing, if not actually supporting the check processing system. Moreover, this level of deposit generation furnishes the most substantial base for credit support enjoyed by corporations.

Different Objectives for Corporations, Institutions and Consumers

Now let us come back again to the problem of competitive self-interest in the emergence of the EFTS. For non-financial corporations four principal areas are affected. The first and most important in terms of dollar value, as we have just seen, and in terms of internal cost, is the processing of vendor payments by accounts payable groups. The corollary of this and of closest interest to the Credit Research Foundation is the processing of accounts receivable remittances arising out of trade sales. The third is the generation of payrolls and other individual payments such as dividends; government payments likewise cover payroll, as well as social security remittances. Finally, there is the vast area of individual payments to corporations for retail purchases, for insurance premiums and for household services such as utility bills.

Taking these in reverse order, it would appear that the emergence of NOW accounts in savings institutions presents the newest and most dramatic competitive element. These have now been joined by point-of-sale terminals sponsored by savings associations in cooperation with chain stores. Commercial banks will need to join this competitive struggle.

The consumer's interest lies first in obtaining cash when he needs it, wherever he needs it; hence, he is a willing user of cash terminals. Thereafter, he is interested in protecting his money as long as possible in some interest-earning institution, hence, his interest in savings banks with their NOW account convenience. He is also intent on spreading payment for his seasonal purchases or for big-ticket items, hence, his interest in department store charge cards. He is equally interested in spreading payments for any number of local stores, and grouping such obligations just as with a department store, hence, his interest in the bank charge card. Above all, he wants to retain control over how and when he makes his payments. He is not at all interested in becoming exclusively bound by any one of these institutional devices.

Nor do these institutions have the same consumer objectives. The savings banks want an average long-run share in the savings dollar in order to conduct their primary business of long-term mortgage loans — and they may extend to other intermediate-term loans as well. The retail commercial banks appear to be looking for a device to generate instalment loan credit. The bank credit card provides its liquidity convenience for consumer purchases to independent merchants and carries a built-in potential for interest income. The department stores are trying to build customer loyalty through credit card services, but also gain the card's use as a customer identification device; and it becomes a means for promoting point-of-sale accounting control in a widespread clerical organization.

Each institution has its interest in EFTS grounded irrevocably in its primary corporate earning objective and the disciplines of its respective accounting system. This is probably why EFTS finds itself right now locked on dead center. It is liable to remain so for an indefinite period, or at least until we have completed the satisfactory automation of consumer accounting systems, and have implemented more point-of-sale terminals in stores and more teller terminals in banks or near banks.

While this may make EFTS seem hopelessly fragmented, and costly because of duplication of effort or under-utilization of local computer switching systems, perhaps this is not all bad, if the consumer is able to get just what he wants and to have access to all the various mechanisms.

Payroll Automation in the Forefront

We are not at all on dead center if we have raised the level of demand of the consumer for more instant or automatic credit of his incoming payments, such as payroll, annuity, and social security payments. The most widespread agents for cashing such checks now have been local food

stores or in some cases, bars. The majority of employees have been reluctant to let their employers make automatic bank deposits for them, and yet there are successful one-check payroll plans around. But, many such deposits have not been truly automatic and people are afraid of mail delay even with local delivery. It is also true they have not had the facility of savings account use for routine payments.

If the campaign has now begun in earnest for automated payroll deposits, this opens the door wide for corporate use of EFTS at an opportune time. Corporate payroll processing has advanced to the stages of general use of automated programs. Many of these have become service bureau generated, or are being consolidated in central corporate payroll centers. Payroll payment systems are dominated by the requirements for maintaining employee accounting records and the generation of withholding records or retirement system records. Data communications facilities have improved and have led to consolidation of payroll record-keeping. More large payrolls are now part of multi-plant or multi-office operations. Now we are confronted with the limitations of issuing and mailing individual checks in a timely manner and EFTS should be the answer. The clerical and computer savings are there to be had, but employee demand for and acceptance of automated payroll depositing has yet to be conclusively demonstrated.

How can he know his pay was deposited, and in the right amount? When he can inquire of his account easily and confidentially by card terminal, perhaps his confidence will grow. But, this is a development that will surely have to be proven. Only when it is widespread, can proposed bill payment services be expected to move aggressively in the electronic funds system. Meanwhile, many forms of payment devices will have a chance to be tried and tested, and we may even have time to work out integrated clearing house switches.

When this does take place, however, corporate deposit float will be the loser. So will corporate payroll accounts at many of the 14,000 commercial banks of the American banking system.

The Biggest Impact from Business-to-Business Payments

Now we come to the primary concern of the Credit Research Foundation, and the concern generally of corporate financial administration with the direction and impact of an electronic payment system. For the past several years, the potential for automating the accounts receivable process has occupied an increasing amount of research time. Within corporate systems development, it is one of the primary areas for computerization and consolidation.

Some useful work has been done to adopt paperless entry methods to cash application of accounts receivable remittances. Lock-box banks have been induced to key remittance data to tape and transmit such trade payment data to corporate computer centers. Certain types of consumer payments, and mortgage payments, have been dealt with successfully in the

same manner, and the BAI has adopted standards for converting and transmitting such payments. However, high volume operations have been too costly in compensating balances, so by now most of these low dollar payments have, in fact, gravitated out of the banks and back to corporate processing centers. The banks have been left with their traditional check clearance role only. This has been propelled by investment requirements in equipment for volume accounting, as with credit cards.

A parallel effort has taken place in accounts payable but, in typical fashion, with little or no reference to the requirements of an electronic funds transfer system.

So we need to come back to the question of who is interested in corporate participation in EFTS for business-to-business payments. Given the substantial deposit generation of the present checking system, who is interested in bringing about a change? Competitively, does anyone have anything significant to gain, or to lose? Who is liable to take the initiative, and at what cost? Is this to be another area where EFTS is fought to a standstill?

How should we distinguish business-to-business payments? For the most part, these are the result of shipments that have gone out from remote warehouses and plants and have been received in the buyer's warehouse or in his plant and must be paid for within a reasonable period of time, usually determined at the time of sale and usually representing an extension of credit by the seller. The permutations and combinations of all the buyer-seller relationships involved in this process, and the geographical remoteness of their respective operations are what give rise to the problems inherent in the business trade payment process. Consumer billing and payment may be accounted for on a balance-forward basis, but trade credit accounting relies on precise identification of all transactions. This is understandably due to their possible complexities with sales adjustments, allowances, or terms, and therefore must be settled on an open-item basis.

The Credit Research Foundation has examined this process in great depth, and has been forced to the conclusion that balance-forward accounting is not a satisfactory alternative. Corporate accounts receivable can only be kept under control by linking the data essential for settlement to the payment itself. In recognition of this fact, it is our conclusion that an EFTS for the American business payment system should be a modified GIRO system, but be geared to many times the volumes characteristic of foreign GIROs, and with much higher levels of automation. It should also be bank-oriented, so transaction settlement will have integrated all money value debits and credits. This would also meet the needs of computerized accounts payable operations.

There is no need here to go into the detailed operations of accounts receivable systems, nor of accounts payable systems. It is sufficient, I think, to indicate that major corporations are actively engaged in applying third-generation computer systems to both areas, and attempting to consolidate each. The developmental cost appears to approximate about \$1

million in each case. In many companies, each major division may have its own accounts receivable system, although this is becoming less and less the case. However, accounts payable operations still tend to locate with production accounting. Receivables control is combined with marketing, order entry and distribution accounting. These are all complex areas and dictate in many instances the limits of adaptation to outside systems.

Six billion yearly payment transactions that consist of paying an average of three invoices each must be managed within the EFTS if we are to take care of the business-to-business segment of the economy. These are represented by \$3.5 billion average sales per business day in the manufacturing segment, \$2.0 billion average per day by retail suppliers, and \$1.5 billion on average for merchant wholesalers. There are over 250,000 vendors supplying 3 million retail establishments. Presently, manufacturers have nearly \$100 billion invested in domestic-trade receivables.

What does this suggest? One concept of the business funds transfer system would have local banks organizing account payable operations for their retail business accounts as an extension of point-of-sale terminal installations. This would appear to be a natural field for commercial banks; but would they care to undertake such a degree of store accounting? If so, will local banks also undertake to extend credit to those retailers as a part of this service? Or, shall we accept the fact that point-of-sale systems will for a long time be geared to customer identification and consumer accounting?

An interesting transformation could be the outcome if credit service were combined with payables accounting. Suppliers ship merchandise under a variety of terms, of which one of the most popular is a 2 percent discount if payment is mailed by the 10th day after date of billing, or net payment is to be made in 30 days. There are many other terms in practice, of course, including the 10th day after the end of the month. There is a rate trade-off implicit in this service area, so it is possible that local banks will supply credit under EFTS payment services that are not now supplied and shift a portion away from suppliers. Under normal circumstances this might be a very favorable influence on retail financial management. In periods of tight money, would it be equally favorable? Surely a dependency could easily develop on the part of store owners that could boomerang under periods of stress.

If local banks do not organize themselves for such service, will retail credit card companies extend their facilities to this field? Or, perhaps, regional factoring companies may expand their scope of practice.

In any event, there is a strong prospect that EFTS services will shift a portion of accounts receivable financing away from trade suppliers. They may even be induced to do so by term incentives. An example of what this would mean is found in the record of June 1970 to June 1971 when there was an easing of the discount rate and the prime rate, and credit became more competitive. Manufacturers' sales increased 3 percent in one quarter, from \$153.3 billion to \$157.6 billion; but receivables investment actually decreased 3 percent, from \$76.7 billion to \$74.4 billion. Because

the length of time receivables were outstanding in relation to average sales had been brought down 2.5 days to 42.5 days, more than \$4 billion of manufacturers's assets were freed for other corporate use.

On the other hand, if local and regional banks or credit service organizations do not take on the initiative of invoice payment, the mere institution of a credit payment system — GIRO style — would have much the same effect. Mail delay and check collection time would be released from the receivables settlement process. It is not necessary for any competitive credit agency to step into this process to gain this effect.

Local merchants and small producers are steadily replacing their manual bookkeeping systems with service bureau accounting. Given the proper controls, this segment of the market may easily participate at a low volume level per bank with bank payments through automated clearing houses. Until nationwide switches are perfected or, perhaps, links are formed through regional banks, this could hardly have a wide effect. Furthermore, it is most unlikely that American business will allow the trapping of GIRO-float within the banking system which would occur if banks did not make prompt electronic payments — another competitive reality to be faced.

Impact of Periodic Corporate Liquidity Problems

This leads us now to the matter of EFTS and its impact on corporate liquidity. This aspect of the problem bothers me far more than all the rest. Through trade credit, major corporations have become a supplier of credit in the economy almost as important as the banking industry. Commercial and industrial loans have been running at the level of over \$118 billion. Manufacturers' receivables are at a level of \$98.8 billion. In a period of tightening money, we might expect a sharp trade-off of credit terms against borrowing rates. Check payments now tend to cushion these adjustments, and receivables accounting is not so quick to detect offenders. Under EFTS and its extension to electronic payments control and receivables accounting, these adjustments could trigger immediate reaction. If corporate collection pressure did not take place, corporate suppliers themselves would be vulnerable to a new angularity in cash flow. If a 2 percent discount is not attractive for prompt payment, an abrupt re-scheduling would be called for to net 30-day payment. This would surely be encouraged by more sophisticated payments management. Under the circumstances, we may need to rethink the whole area of the funds value transfer in business term disciplines.

Angularity and peaking in cash flows will take place in any event if EFTS comes into existence under the present pattern of billing terms. When the rate trade-off becomes pronounced, non-financial corporations will be greatly dependent on the availability of demand credit, and will force any credit expansion pressure back into the banking industry. Time deposits and CDs in banks would feel the rate trade-off effect. Will banking be as able to accommodate this expansion on a demand basis if EFTS

practices have dropped deposit float support out of the balance structure? Would the Federal Reserve System support such expansion of credit? Or is the Fed presented with a sharper instrument of credit control? Beyond the banks, this liquidity pressure would have its effect as well on the magnitude and timing of corporate short-term investments, the only alternative for immediate liquidity.

We see a very perplexing period ahead for business corporations in attempting to adjust to an Electronic Funds Transfer System. It goes well beyond the implication of fewer checks to process.

In summary, there are interesting prospects under EFTS for the development of new competing services to replace check processing, and new competing institutions. Overall, that is undoubtedly a healthy sign. On the other hand, warning flags are in the air that adjustments in basic working capital management will need to be made by corporate financial administrators. These may be more significant hurdles to overcome than the problems of bare automation design. There are, of course, problems of systems controls for all participants as documents disappear. But there are also important problems to be resolved in re-adjusting traditional credit markets, and the constraints to be imposed on EFTS-related credit practices.

Finally, I don't think there is any way to prevent this EFTS from developing as an open system. Competition and strong self-interest will assure that it is. It is a pleasure to participate in this examination of some of the foreseeable consequences.

Discussion

Richard F. Kerr

Good morning! It is traditional to say that it is a pleasure to be here — and indeed it *is* — the setting is magnificent, the fellowship great and the conversations and discussions stimulating.

I am flattered and honored to be asked to discuss Dick Dundore's paper and to present my own views on the Electronic Funds Transfer System and its implications for non-financial corporations, particularly retailing, even though I realize that the invitation was tendered only because of a "Tell-It-Like-It-Is" presentation which I made at the annual meeting of the Bank Card Division of The American Bankers Association in September, 1973. The views expressed in that presentation, as well as those expressed today, are mine, alone, and do not necessarily represent either the policies or philosophies of Federated Department Stores or other members of the National Retail Merchants Association.

Much has happened in the field of Electronic Funds Transfers since September, 1973:

1. The Federal Reserve Board asked for comments from a broad spectrum of financial and non-financial institutions concerning proposed changes in Regulation J — and I suspect that the Fed was overwhelmed with the 243 responses.
2. The myth that the rising volume of checks would bring about a collapse in the collection system has been exploded.
3. Retailers have installed, or ordered, about 80,000 point-of-sale devices.
4. Legislation concerning EFTS has been introduced in the Congress.
5. Arthur D. Little, Inc. held a Technology Assessment Conference on June 13, 1974, at which all groups interested in EFTS, except the Department of Justice, were represented.
6. Almost every conference of financial and non-financial institutions has had at least one speaker, along with discussions, on EFTS.

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With the exception of the Technology Assessment Conference and this one, at which "the spirit of open inquiry and mutual assistance" was, and is, quite evident, the other conferences have all dealt with emerging competition and the actions which must be taken by the interested parties to assure who, as Dick Dundore says, "will best capture the most consumer participants and their household accounts."

Why this sudden change in EFTS attitude and effort? It seems to me that there are three reasons, all of which involve self-interest:

1. It represents another example of the continuance of the traditional free enterprise system.
2. No one wishes to be excluded from direct participation in this, the payment system of the future.
3. There seems to be a newfound realization that commercial banks have no God-given right to control the payment system.

In effect, what I have said so far leads me to believe that Dick and I have very few differences in our views towards the implications of EFTS for non-financial corporations and those that we do have are probably just a matter of degree.

As a matter of fact, I found his paper to be interesting, informative and extremely well-organized. Unfortunately, from a retailer's consumer-credit point-of-view, the paper is concerned, primarily, with the impact of EFTS on the administration of business-to-business payments. However, the possibilities and problems associated with any implementation of this important part of EFTS certainly needed the expert presentation made of the in-depth examinations conducted by the Credit Research Foundation.

As an ex-manager of an accounts payable operation, processing invoices from 40,000 vendors for a large department store, I'd like to draw your attention to, and emphasize, just one of the problems of this business-to-business (merchant-to-vendor) payment mechanism:

As Dick Dundore said:

The permutations and combinations of all of the buyer-seller relationships involved in this process, and the geographical remoteness of their respective operations are what give rise to the problem inherent in the business trade payment process.

For example, retailers have always had problems with coordinating shipments from a vendor's remote warehouses or manufacturing facilities with invoices which were forwarded separately from the vendor's central accounting office. The introduction of electronics into vendor invoicing and data line communications between the vendor's remote warehouse, or manufacturing facilities, and invoicing office has only compounded the problems. We now receive invoices days and weeks before receipt of the

shipment and, even though the invoices may be post-dated, the cash discount payment terms may have expired before we receive the merchandise. Frankly, our experiences with shipment shortages, overages, substitutions and damages have indicated that it is not prudent to pay until the shipment has been received and checked.

This kind of problem is the reason why "credit trade accounting must rely on precise identification of all transactions." In other words, both corporate accounts payable *and* accounts receivable can be kept under control only by linking the data essential to the payment made and received, and, because of this, I doubt that either an EFTS, or a modified Giro, are satisfactory substitutes for the present cumbersome system, unless, of course, they could be modified to include the precise identification needed for control.

Therefore, I believe that the business-to-business payment mechanism will be the last to use a point-of-sale electronic funds transfer system.

Even though that sounds very final, I cannot leave the subject of business-to-business payments without noting that I became extremely interested in some of the concepts of the use of EFTS for the business payment system, particularly those involving bank organization of retail accounts payable systems and the bank financing of retailers and the huge amount of domestic trade receivables. I think that, at the very least, these concepts are certainly worth exploration and investigation by the managements of banks, retailers and vendors.

And now to my favorite subject, my chosen profession, my life's work, retailing and people, real live people, not pieces of plastic or cardholders, for retailing relates better to people, in an attempt to satisfy their wants and needs, than any other major industry.

I have been fortunate to be employed by Federated Department Stores, the nation's largest and most profitable group of department stores, for the past 25 years. Right now, I am involved not only in the entire customer credit operations function at Federated, for which I get paid, but also in the other end of the customer credit function, through the National Foundation for Consumer Credit — which is a labor of love, that of consumer credit education and the credit counselling of those unfortunates who have become overburdened with debt. For therein lies the dilemma of all of us who are credit grantors — on the one hand we are accused of overburdening people with debt and on the other hand we are accused of restricting the availability of credit — particularly to those of low income or those who are inner-city residents, but in either case, those who need consumer credit the most.

With your permission, I am going to take this fundamental dilemma, add to it what we believe our customers think about payment services, what retailers are doing with point-of-sale devices and why, throw in a little philosophy, mix them all together and try and relate the resulting stew to the implications of EFTS for retailers, particularly large department stores.

During the last two years, retailers have become increasingly aware of the possibility of a bank-operated EFTS and increasingly concerned over the related possibility of bank control, through EFTS, over the credit information and credit granting industry. Their position is best described by the Report of The National Commission on Consumer Finance, page 213:

Finally, the emergence of the electronic funds transfer system means that whoever controls and operates that system will also have a record of credit extensions and payments. Consequently, if commercial banks continue to enlarge their share of the consumer credit market and if the bank card-EFTS becomes a reality, commercial banks will not only control the funds transfer system but they will own the major portion of the available credit information. Moreover, banks will be under no obligation to share credit information with competing firms whose own credit information will become progressively less reliable as banks enlarge their share of the market. In short, if the banks' current dominant role in credit cards is coupled with control of the EFTS and, by extension, ownership of the credit information system, those banks dominating these systems will be in a position to exercise significant control over the market for consumer credit. If only two credit card plans emerge as part of EFTS, a large and growing portion of consumer credit in the United States will be controlled by a two-system oligopoly with a potential for restraint of competition in the market for consumer credit.

The Commission characterized this possibility as "an intolerable result in consumer credit" (Report, page 208).

Of course, that may be an overstatement and retailers may very well be over-concerned about the possibility but, as a matter of self-interest and competitive survival, they should have some concern. As NRMA stated in its comments concerning Regulation J, "If commercial banks, in time, control the electronic mechanisms for pre-authorization payment, DDP, POS and credit information systems retrieval, what would be left as an inducement for the consumer desiring credit to apply for and utilize the facilities of the general merchandising retailer? The commercial banks would be the repositories, non-competitively, of data on the personal and financial lives of the consumer."

Now even though I cannot envision this as even a possibility, it does represent a good illustrative implication of the great dilemma — too much credit for some and too little credit for others — for, on the one hand, the substantial lines of credit offered by bank credit card plans may encourage some customers to become overburdened with debt but, on the other hand, bank-credit-granting standards appear to be much more conservative than those of retailers and other credit grantors.

As a matter of fact, retailers have known for years that most consumers have established their first credit accounts at their local department stores. With bank-card control over EFTS and the credit information system, where would the young or marginal customer be able to obtain credit? If the answer continues to be the local retailer, would he be able to continue to offer consumer credit, or even stay in business, realizing that, ultimately, his credit customers would be only those unable to obtain, and become a part of, the bank credit-card part of EFTS?

Should this happen, the retailer has three choices:

1. He can raise prices, become less competitive and lose those customers who are able to obtain credit from other sources.
2. He can accept bank cards and sell for cash and lose those customers who are unable to qualify for a bank card.
3. He can operate a "cash only" business and really lose customers.

From a sociological viewpoint, the first choice might be the best in the long run, for it is the only one which does not prevent the entry of millions of customers into the credit part of the payment-services system.

What do consumers think about EFTS? Not much! Their understanding of it is miniscule. All they know is that it involves computers and, in the beginning, all of us made certain, in our own inimitable ways, that customers would not like computers. We made errors, and didn't correct them promptly, we didn't change addresses fast enough, we updated our files periodically instead of daily, we dunned them for payments when we should not have, we did not process credits promptly and we dehumanized them by treating them as numbers.

More recently, we have learned to manage our electronic systems better. We do not make as many mistakes, and when we do, we correct them promptly, and, at least in retailing, we are processing fewer bill complaints and inquiries than ever before and our customers have accepted, perhaps reluctantly, our systems.

However, people continue to believe that computers are inhuman — too big, uncontrollable and too knowledgeable — and they do have long memories. So, when asked about EFTS, most of them say, in the New York vernacular, "Who needs it?" And the more sophisticated say, "What's in it for me?"

And why shouldn't they answer this way? They are perfectly happy with their present payment systems, they don't understand EFTS, with its viable alternatives and added convenience, because it has not been sold to them.

Consumers want access to, as Dee Hock says, "value exchange," 24 hours a day, 7 days a week. To retailers, that means access to merchandise and services, and retailers have attempted to react to the demand. In most locations, except where there are Blue Laws, our stores

have been open 7 days and 6 nights each week for several years, and in most metropolitan areas, merchandise can be ordered by telephone, 24 hours a day.

With the advent of automated tellers and cash dispensing machines, commercial banks have also reacted to this demand. In fact, some banks are now open on Saturdays, and that is almost heresy.

The thrift institutions have reacted, too, and have answered the "What's in it for me" question with their *NOW* accounts and *PLAN* accounts, and the success of the Hinky Dinky experiment proves to me, at least, that customers want to be able to make *deposits* during non-banking hours.

Thus, through the imaginative, competitive use of electronics, it appears that financial institutions are finally reacting to customer demands for almost continuous access to their "value exchange."

What are large retailers doing about electronic cash registers or point-of-sale devices? They are ordering them in huge quantities and installing them as rapidly as they are produced and delivered. Why? To better satisfy their needs for merchandise information, to simplify the calculations made for total merchandise price and taxes and to better identify and approve any credit purchases made. They are not designed to just handle a cash sale, a cigar box could do that. In addition, they are less expensive than the large mechanical registers ordered in recent years.

Retailers are not ordering the type of black box POS device, envisioned by some bankers, into which a piece of magnetically encoded plastic is inserted, the transaction data and a secret code are entered and the desired results achieved electronically.

Retailing's major problem is *not* with a technology for reading our credit cards, but *is* with the technology required for reading our merchandise tickets. Basically, we need a device with a hand-held reading capability — and our merchandise tickets must be machine and optically readable by a customer and the salesclerk. In addition, the merchandise tag must vary considerably in size. We need tags that stick to merchandise, can be pinned or clipped to goods or can be hung from merchandise. Above all, our tickets must be inexpensive. This last is the real rub at the present time, as it appears that magnetic technology is too expensive.

Thus, while banks appear to be going down the magnetic path, retailers are tending toward an optical font, bar code or punched hole — in fact, we are headed in almost every direction *but* magnetics.

This is what I said a year ago and I still believe it, but *Women's Wear Daily* on September 30, 1974, stated:

The universal sales ticket scheduled to be introduced by the NRMA next month is expected to raise questions about whether retail and apparel manufacturers can afford the project.

Some retailers say that the standard ticket — which took five years in planning — is expected to take another five years in implementation.

Quoting Donald Hurlbert, Director of Information Systems for Belk Brothers Stores, *Women's Wear* reported:

Originally the cost of OCR-A wands were listed as \$600, and then it went to \$1,000, and the last time I heard about it the price was over \$1,500. There are not that many stores that can afford to have an additional \$1,500 expense at every cash register.

Where does this latest development leave retailers? Right where they are today, using the capabilities of the ECRs by continuing to require sales personnel to enter the information manually so that it can be controlled and reported electronically, for increased sales and profits.

What is retailing's interest and involvement in EFTS? We have had lots of interest, but very little involvement, so far.

Frankly, we have developed no thrust for dealing with an EFTS. We have been, and remain, interested observers:

- We have noted the concept of an EFTS evolves from a bank-card-oriented system to a total payments mechanism.
- We have noted that financial institutions appear to be jockeying for position in what they refer to as an "emerging" EFTS.
- We observe financial institutions more willing to discuss EFTS implications for the consumer and, hence, our business, and we find this encouraging.

Up to now, we have viewed an EFTS as commercial banking's solution to a commercial banking problem:

- As "partners", we know that "your" system will have its effects upon our customers and our business, and
- When research and fact override fear and emotion, we are confident that "your" EFTS will give due consideration to our needs as your "partners" . . . the customers we share and our business.

We recognize that an EFTS must address itself to many complex problems in dealing with our business:

- Up to now, the retail industry has been relatively free from regulation. Consequently, no two department store chains operate in the same manner. Our businesses can differ greatly in accounting,

auditing, budgeting, costs, credit plans, equipment, merchandise assortments, personnel requirements, policy, reporting, security, space, standards, supplies used and systems and procedures.

- Our use of computer technology has been addressed primarily to handling our business "as usual" . . . but faster. In this area we have not been innovative. We remain relatively unsophisticated. Interfacing with a complex system will not be easy.
- In numbers, most stores, are not automated. Manually interfacing with computers poses some very real cost problems.

As processing payroll and customer payments are a minor problem for stores, we cannot devote major effort to, or suffer major upset because of, changes in these areas . . . unless duly compensated.

Should an EFTS impair our relationship with our customers . . . credit and/or cash . . . we would take a close, hard look at what could be a major problem.

If the effect of an EFTS were negative in this regard, we would be forced to fight for survival.

Frankly, we have serious doubt that an EFTS . . . from what we have observed . . . will be accepted by our customers.

Consumers do *not* handle their affairs in a disciplined manner. We are not sure they now spend even the time required to participate in a disciplined handling of their finances. If this is so, advantages to the consumer of a total POS-EFTS, with its automatic elimination of float, will be extremely difficult to sell, particularly if you persist in using such acronyms as *COPE* and *SCOPE* and now, *GACHA*, (Georgia Automated Clearing House Association) the worst of all. The connotation will not be misunderstood by consumers.

In summary, therefore, retailers look to banks to do the research, develop the systems and conduct the experiments. We are quite willing to fill out questionnaires, explain our business and otherwise assist . . . if our cost is low. If our customers like your system, we'll buy it at a cost dictated by our customers. If customers don't like your system and/or its cost, we will be forced to look for alternatives.