Still Paying with Paper

Small businesses continue to write and receive checks

Research Brief
October 2012
Introduction

The number of consumers using checks in the U.S. has progressively declined during the past decade. Today, many favor electronic payments instead. Recent statistics from NACHA – The Electronic Payments Association – reveal that consumers pay 500 million bills per month using Direct Payment via ACH. Consumer research completed by FIS™ in 2012 notes that online bill payments and pre-authorized ACH debits account for 49 percent of all recurring bill payment volume while checks comprise only 21 percent. Although consumers have demonstrated notable progress in migrating away from checks, check payments make up a significant portion of business payments.

The “2010 Federal Reserve System Payments Study” shows a tremendous decline in consumer-to-business checks from 17 billion written in 2006 to 12.3 billion written in 2009. In sharp contrast, business-to-consumer checks declined by only 0.4 billion – from 5.6 billion in 2006 to 5.2 billion in 2009. Also, business-to-business checks declined by only 0.4 billion – from 8.3 billion in 2006 to 7.9 billion in 2009. The smaller declines are quite apparent among businesses, which are keeping check writing alive.

The research driving this white paper shows that small businesses in particular tend to use checks to send and receive payments across lines of trade. According to the survey, nearly half – 46 percent – of all check usage involves a small business, which presents opportunities for financial institutions to help this unique segment migrate away from checks and ultimately increase overall adoption of electronic payments.

Payroll – how businesses pay their employees – emerged as a prominent area of opportunity. Payroll currently contributes 2.7 billion checks to the overall check volume. A shift toward Direct Deposit via ACH would create significant operational, cost and even result in environmental benefits for small businesses. Currently employing 43 percent of the U.S. workforce, small businesses have an opportunity to motivate this large segment and also influence consumer payment behaviors. By adopting electronic payment options, small businesses can promote electronic payments beyond how they pay their employees to how their employees, in turn, make payments.

Small businesses transact with other businesses of all sizes. Depending on factors such as the need for goods and services to do business, the frequency of business-to-business payments varies greatly. Regardless of business size and frequency of transactions, the 41 percent of small businesses currently paying other businesses with checks represents opportunity for migration to other payment options such as Direct Payment via ACH.

The perception about electronic payment options is very important among small businesses as well as among consumers and business customers. The research driving this white paper reveals that not all small businesses feel they have the scale and scope to adopt, or offer, electronic payment options. Financial institutions can help shift such perceptions by working with small businesses to identify appropriate products and services. The options available for businesses of all sizes are numerous. Certainly, no business should feel as if it is too small in terms of revenue or number of employees not to consider electronic payment options. That shift, however, begins with a change in perception among small businesses and their customers.

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Survey Methodology

In November 2010, FIS and NACHA jointly conducted a 51-question online survey to understand payment behavior among small businesses in the U.S. The research also explored small businesses’ usage of electronic payment products and services and the relationship between Direct Deposit via ACH and other payment forms, in particular.

Organizations defined as small businesses met the following criteria:

- Employed more than one individual
- Reported revenue of less than $20 million in 2009
- Used a business checking account and not a personal checking account as the primary business account

Respondents’ professional roles within small businesses were limited to owners, chief executive officers or presidents, chief financial officers, controllers or treasurers, office managers, accountants or bookkeepers. Self-employed individuals operating unincorporated small businesses, which may or may not be the owner’s primary source of income, were not included in the survey. The sample size of the survey was 2,249 small businesses.

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Small Businesses in the U.S.: Payment Footprint, Practices and Perspectives

Overview
Small business has a sizeable presence in the U.S. and generates 25 percent of total annual sales on average. Also, 43 percent of the U.S. workforce, including individuals who are self-employed, is employed by organizations with less than $20 million in annual revenues according to estimates based on U.S. Census Bureau and U.S. Bureau of Labor Statistics data. However, a surprising 46 percent of overall paper check use involves a small business (Figure 1). Small-business-to-small-business transactions account for nearly 25 percent of check use, while consumer-to-small business payments constitute 10 percent, and small business payrolls add 12 percent.

Figure 1: Small businesses account for 46% of all non-government checks written.

Distribution of all checks written annually in the U.S., not including checks to or from government

Consumer Preferences
Small businesses accept payments in many forms, which are often dictated by how consumers choose to pay for goods or services. Almost one-third of payments received by small businesses are in the form of checks (Figure 2). Credit and debit cards are the second-most common form of payment constituting 28 percent of the total. Such transactions tend to be associated more with consumer-facing small businesses such as retail stores. Interestingly, consumer-facing small businesses also receive the most cash-based payments – 19 percent. The remaining 22 percent of payments received are in the form of preauthorized ACH credit and ACH debit transactions, prepaid card and wire transfer payments. In total, paper-based payments, including checks and cash, account for half of all payments received by small businesses.
Small Business Types

Consumer-facing small businesses, which comprise 30 percent of all small businesses, include retail stores, accommodations (restaurants and hotels) and personal care establishments (barbers, beauty and nail salons, gyms, etc.). These organizations are more likely than small businesses in other segments to accept a variety of payment forms (Figure 3). Approximately 90 percent of these small businesses accept checks, cash, and credit and debit cards as forms of payment. Conversely, only about 50 percent of small businesses in other segments accept cash and credit and debit cards. They opt for checks instead.

Figure 2: Paper payments account for half of payments received by small businesses.

<table>
<thead>
<tr>
<th>Payment Type</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Check</td>
<td>31%</td>
</tr>
<tr>
<td>Credit &amp; Debit Cards</td>
<td>28%</td>
</tr>
<tr>
<td>Other Payments</td>
<td>22%</td>
</tr>
<tr>
<td>Cash</td>
<td>19%</td>
</tr>
</tbody>
</table>

Source: FB & NACHA, November 2009. n = 2,269 small businesses.

Other Payments include ACH, credit card, wire transfer and Internet/P2P payments.

Figure 3: Retail-oriented small businesses generally accept all payment types; checks dominate over cash and cards in all other industries.

Source: FB & NACHA, November 2009. n = 2,269 small businesses.
Customer Types

Customer mix also has a significant effect on the types of payments small businesses receive (Figure 4). Small businesses transacting with other businesses are found to receive the most checks. This finding is expected because business-to-business transactions tend to be specific and occur infrequently compared to transactions between small businesses and customers. When small businesses are paid by the government, 52 percent of payments fall into the “Other” category. Since the government does not make cash payments, checks are common. Checks represent more than one-third – 36 percent – of payments made by the government to small businesses. Only 24 percent of consumers paid small businesses with checks. One-third of consumers pay using credit or debit cards, which can be a result of associated loyalty and reward programs offered by retailers. Among consumers, cash (26 percent) and checks (24 percent) vie for second place.

Payment Frequency and Value

A closer look at aspects of payments, including frequency and value, shows such factors also affect payment types across industry segments as well as customer types (Figure 5). Small businesses that receive fewer and larger payments are less likely to seek the convenience of credit and debit cards. Two-thirds – 65 percent – of payments originating from such customers to small businesses are made with checks. Conversely, small businesses that frequently receive payments of smaller value are less likely to receive checks as a form of payment. Only 35 percent of such payments are made with checks. Large payments, regardless of customer and industry segment type, are more likely to be made by check.
Naturally, the forms by which small businesses pay their bills can indicate how they receive payments as well. Typically, small businesses pay more of their bills by using checks rather than other payment forms (Figure 6). More than half – 51 percent – of small business payments are made with checks. Payroll checks comprise 22 percent of small business payments. Payment by credit or debit card is the next most common method – 16 percent – followed by online bill payment at 9 percent.

**Payment Practices**

**Figure 6: Checks account for half of the payments made by small businesses; card-based payments account for 20 percent.**
The payment frequency and value associated with how small businesses receive payments, however, does not translate into how they pay their own bills. Being the preferred payment form, checks are common. However, the size of a small business reveals a minor effect on choice of payment form (Figure 7). For small businesses with annual revenues of less than $750,000, 42 percent of payments are made with checks. For larger small businesses with revenues exceeding $5 million, 57 percent of payments are made with checks.

Figure 7: Checks account for the largest portion of payments made for all sizes of small business.

Small Businesses in the U.S.: Challenges and Opportunities

Controlling cash flow and costs are critical to the health of a small business. Faster receipt of payments and more control over timing of bill payment through electronic means both facilitate cash flow. Reducing operational costs associated with inefficient payment methods assists small businesses in their ability to focus on their core competencies to grow their businesses.

Challenge

Small business payroll accounts for 12 percent of overall check use. This seemingly small percentage, however, equals about 2.7 billion checks per year. For small businesses with less than $1 million in annual revenue, payroll checks represent the majority of checks they write (Figure 8).
Opportunity

Organizations with less than $20 million in annual revenues and individuals who are self-employed constitute 43 percent of the U.S. workforce, according to estimates based on data from the U.S. Census Bureau and U.S. Bureau of Labor Statistics. Direct Deposit via ACH can help small businesses realize operational and cost efficiencies, depending on the number of employees and also the number of employees who opt for Direct Deposit via ACH. Smaller businesses are perhaps less likely to offer Direct Deposit via ACH to their employees versus larger small businesses because of their possible misconception that it is a costly proposition. An overwhelming 83 percent of small businesses with revenues between $5 million and $20 million offer Direct Deposit via ACH while only 28 percent of payroll accounts are paid via check (Figure 8).

Small businesses that are able to pay their employees through Direct Deposit via ACH can save $150 – $300 annually, per employee, depending on the total number of employees. Additional benefits of Direct Deposit via ACH include improved operating efficiencies, increased productivity, and an opportunity to impact the environment positively by reducing the amount of paper in circulation.

Small businesses offer Direct Deposit via ACH specifically at the request of their employees, thereby increasing employee satisfaction and retention. A majority – 86 percent – of organizations view it favorably as well, which is strong evidence that cost and operational efficiencies are values that many organizations and their employees seek (Figure 9).
Challenge
More than half of small businesses – 51 percent – pay their bills using checks. Also, one-quarter of small businesses pay other small businesses with checks.

Opportunity
As electronic payment methods are promoted among small businesses for bill payment, this will ultimately drive increased awareness of electronic payments and influence how they are paid by other small businesses.

Challenge
Three out of 10 small businesses are retail/consumer-facing. These include retail stores, accommodations (restaurants and hotels), and personal care establishments (barbers, beauty and nail salons, gyms, etc.). Ninety percent of these small businesses offer diverse payment options for consumers. However, only half of the remaining 70 percent of small businesses in non-retail segments offer as many payment options (Figure 3).

Opportunity
Small businesses in non-retail segments represent prime targets for simple, low-cost electronic payment options that provide the dual benefits of encouraging their customers to migrate from cash and check payments and enable the small business to realize operational and cost efficiencies.

Conclusion
Tremendous opportunities exist for small businesses to diversify their payment offerings – to both send and receive payments electronically – and ultimately realize cost and operational efficiencies. However, many small businesses feel that they do not have the size or infrastructure to realize the benefits of electronic payment options such as
Direct Deposit via ACH or Direct Payment via ACH. Furthermore, some consumer and employee segments prefer using cash or checks to make and receive payments. Finally, there seems to be an educational gap about electronic payment options appropriate for small businesses. Figure 10 highlights several reasons why small businesses are not adopting Direct Deposit via ACH. Note that one-quarter (26 percent) of small businesses have never been approached about using Direct Deposit via ACH.

**Figure 10: Beyond assuming the business is too small, employees preferring checks/cash and never being approached are also top reasons for not adopting Direct Deposit via ACH for payroll.**

<table>
<thead>
<tr>
<th>Reason</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have too few employees to justify it</td>
<td>46%</td>
</tr>
<tr>
<td>Employees prefer receiving checks and/or cash</td>
<td>28%</td>
</tr>
<tr>
<td>No one has ever approached the company about using Direct Deposit via ACH for payroll</td>
<td>26%</td>
</tr>
<tr>
<td>Direct Deposit is too expensive</td>
<td>21%</td>
</tr>
</tbody>
</table>

Source: FB & NACHA, November 2009; n = 2,249 small businesses

Tools and resources such as NACHA’s ElectronicPayments.org can help educate small businesses and customers about the benefits of different forms of payment, including Direct Deposit via ACH and Direct Payment via ACH. Importantly, the signals small businesses send to their customers by offering electronic payments can bring about systematic change and influence how payments are sent and received within the larger business community. Finally, small businesses can speak to their financial institutions or payroll providers about the benefits of Direct Deposit via ACH and implementation possibilities.
About FIS

FIS (NYSE: FIS) is the world’s largest global provider dedicated to banking and payments technologies. With a long history deeply rooted in the financial services sector, FIS serves more than 14,000 institutions in over 100 countries. Headquartered in Jacksonville, Fla., FIS employs more than 32,000 people worldwide and holds leadership positions in payment processing and banking solutions, providing software, services and outsourcing of the technology that drives financial institutions. First in financial technology, FIS tops the annual FinTech 100 list, is 425 on the Fortune 500 and is a member of Standard & Poor’s 500® Index.

For more information about FIS, visit www.fisglobal.com.

About NACHA — The Electronic Payments Association

NACHA manages the development, administration, and governance of the ACH Network, the backbone for the electronic movement of money and data. The ACH Network provides a safe, secure, and reliable network for direct account-to-account consumer, business, and government payments. Annually, it facilitates billions of Direct Deposit via ACH and Direct Payment via ACH transactions. Used by all types of financial institutions, the ACH Network is governed by the fair and equitable NACHA Operating Rules, which guide risk management and create payment certainty for all participants. As a not-for-profit association, NACHA represents more than 10,000 financial institutions via 17 regional payments associations and direct membership. Through its industry councils and forums, NACHA brings together payments system stakeholders to foster dialogue and innovation to strengthen the ACH Network.