Is it the right time for collection agencies to rethink their business models?

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It was at an ACA Annual Convention workshop on employee compensation that I was motivated to ask myself some interesting questions about the way collection companies are managed and operated today. I think it would fair to describe the average owner or collection manager as conservative and conventional. For most, although everything around them is changing rapidly, the basic business process has not changed in many years. Although some radical thinking does exist, it is often the exception. That is not a weakness - change is often difficult and costly.

This discussion was intended to provoke dialogue and questions about different business models in the collection industry. The thoughts presented are based on many years of collection experience as well as a unique opportunity I have had to introduce radical thinking to the industry.

Compensation

Let us start with the concept of compensation. The conventional wisdom is that we pay people for collecting money. Almost every compensation model in the industry is based on that model. It may have worked when we were collecting 35% at rates of 50%. But is it the best approach in this new era of collections? Should we start paying people for finding the debtors who do not pay? Why should we consider such an outrageous idea? Would the following justify it?

- Over 75% of accounts are *not* collected
- It is easier to find a person who will not pay than a person who will pay
- Every non-collectable account that is identified quickly allows us to devote more resources to the collectable accounts
- If less than 25% is collected, why (and at what cost) do we put the *same* effort into the other 75%?

Some of the existing models do attempt to limit commissions paid to collectors if the payments are generated prior to an account being worked by a collector. That makes sense, but what about the accounts that are eventually worked by collectors? Should we compensate a collector in a *different* way if an account is more collectable? We usually do not. What if we could identify accounts that are more likely to pay? We would not even need experienced collectors to work them initially. Of course this is a different business model, but one that has to be considered as we try to collect more at a lower cost.

Finding the people who will pay

As we consider different aspects of a collection operation, the experienced manager will realize that a collection operation is not a matter of simply bringing together areas such as people, a few large clients, technology, scoring, automated dialing, collector compensation and client services. All the different facets of an operation are related and tied together by a single important (and often neglected) item – your business model. The area of scoring is a great example of the value of the business model.

With “scoring”, we are trying to determine who is most likely to pay. Eliminating even a small percentage of the large numbers who are *not* likely to pay will also help to isolate the possible payers. We could then use our results to classify our accounts from highly collectable to least likely to pay. How do we score accounts?

- We obtain “external” scores
- We use the (internal) information and knowledge we already have within our systems and companies
- Collectors and managers make individual judgments

Why do we continue to give up on accounts because they are small? That has to be a poor scoring model - Talk to companies that collect parking tickets! We *must* begin to focus on a collection model that is primarily based on collectability. We *can* classify every account and focus our efforts on the 60% who are most likely to pay. What about the other

40%? Many clients will not want to see their accounts closed within 24 hours even if *they* knew that they would never collect on them. Because people cost much more than letters, we must consider working those accounts using mail as opposed to telephone calls and contacts, making sure that they are never overworked. And how do you do that? It is simple – you automate, automate and automate.

If we put less effort into less collectable accounts we will need fewer collectors! Those collectors would collect more money and would consequently demand higher commissions. We need to revisit our business model. If costly technology is applied to predict paying debtors, the compensation models will have to change.

Dialers

Today, the automated dialer is established, accepted and mature technology within the collection industry. In spite of its productivity, many of us still do not have a business model with a high percentage of predictive calling. Why? It is because we know that people will collect more when they are "responsible for an account" for a longer period. A good collector will always collect, and given the choice of working a few more accounts a day and taking home a little more money, they will probably say "Yes".

So why not take your large balance collectors, change the ownership model and let them work in a pooled environment? It is probably because most of us cannot measure individual productivity in a pooled environment. If we could do that *and* find a way to allow collectors to hold accounts for just enough time to collect on positive contacts, we could improve collector motivation and increase contacts by 100% compared to an ownership model with no predictive dialing. Yes, we need to go back to rethinking our business model. And when collectors make many more contacts, they will probably collect more. Do we pay them more because of your investment in technology? It is interesting how we keep coming back to the issue of compensation.

Dialers need to be a part of our business model. Today, they are not.

- Dialers must work without being managed in terms of the accounts to be called each day or the pacing of the calls.
- We must find ways to improve the quality of the numbers we send to the dialer. Bad numbers must be removed quickly from calling lists.
- We must dial responsibly - predictive dialing must not be allowed to become a liability.

Some other areas where change could be beneficial

In addition to the above, there are several other areas that merit attention within a business model. Some of these are:

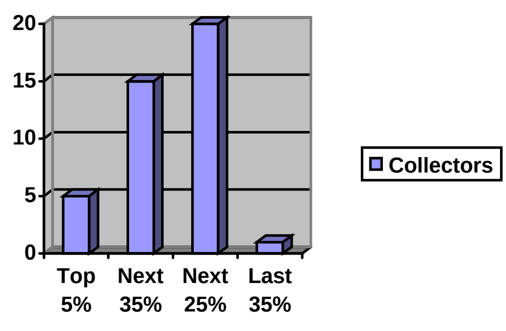
- If automation plays a greater part, a collector's role could be reduced to "working their accounts". Decision-making and thinking *must* be consistent and should be controlled *by management* as opposed to individual collectors.
- How do we give credit individuals when multiple people (e.g. collectors, skip tracers, insurance billing staff) were involved in generating the payment?
- We must *<u>not</u>* be forced to manage workflows or ensure due diligence with human resources. These are jobs where computers excel.
- Automation has not always made our jobs easier, improved service or saved on expenses. We must address these areas using technology.

The operation under the new business model

If we changed our business model, how would the traditional agency change? Let us consider a company with 50 collectors and 5 supervisors. We have analyzed and classified the accounts based on collectability. We will not need experienced people to work the most collectable accounts, and the least collectable accounts will be worked with the least effort being expended. In the new business model, our collection operation could possibly look like the following.

- After the initial letter efforts 5 collectors with limited experience could handle the early efforts on the 5% of accounts classified as most collectable. They could be salaried employees who are not paid a commission. Some of you may disagree with this and believe that your best collectors should work your best accounts. That is a valid argument.
- About 15 experienced collectors would handle the next 35% of accounts classified by collectability. These collectors would be on a salary plus commission, but quotas would need to be adjusted, based on the higher fees they should generate.
- There will be about 20 "account representatives" who handle the next 25% of the classified accounts. They do *not* have to be experienced collectors since the accounts are not likely to generate many payments.
- The last 35% will be worked by the system with letters and calls (when absolutely required) being handled by the same 20 account representatives.

The following represents the collector allocation by collectability "segment".



As you can see, the new model calls for 40 collectors compared to 50 in our traditional model. We may be able to manage with one less supervisor too. In addition to the reduced numbers, the costs are lower because we do *not* require experienced people in every area.

How do we start if we wanted to change?

In addition to changes in management thinking, you will need new tools to implement progressive workflows and higher levels of automation. In the 1990's several major companies were challenged to redesign their business processes. IBM reengineered their operations while the automakers invested in technology such as robotics. For collections, it is unlikely that traditional software models will provide the power and depth that is required. The most cost-effective solutions will probably utilize knowledge-based technology. This technology uses stored knowledge to provide flexibility, allowing you to frequently change your logic for scoring accounts or adjusting your work plans without the need for programming changes.

The ideas presented may seem radical to some of the readers but they have been tested and implemented with exceptional results. Where do we go to find the next great increase in productivity? We have always looked to technology but that may not be the only answer. After nearly 25 years of automation, perhaps it is time to take a new look at how we would design our solutions if we had to do it today. And it all starts with a business model.

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