



SAP White Paper



# **PROTECTING PROFIT MARGINS THROUGH AUTOMATED CHARGE- BACK MANAGEMENT SOLUTIONS**

THE BEST-RUN BUSINESSES RUN SAP™



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## **EXECUTIVE SUMMARY**

Wholesale distributors rely on rebates, or chargebacks, from manufacturers to protect their profit margins. However, many distributors don't claim all of the funds to which they are entitled because their manual procedures are prone to error. This narrows margins and negatively affects profits. Using an automated chargeback management solution, wholesale distributors can eliminate errors, ensure that they file claims for all rebates due to them, and improve the quality of information used for making business decisions.



## **PROTECTING PROFITS WITH EFFICIENT CHARGEBACK PROCESSING**

Wholesale distributors compete based on their pricing strategies, and they rely on back-end rebates, also called chargebacks, to protect their profit margins. Let's say a manufacturer offers a product to end customers at a price less than a distributor's cost. The manufacturer reimburses the price difference to the distributor after the distributor files a chargeback claim.

It's income to which a distributor is entitled, but many distributors give away this back-end money simply because they use manual, error-prone processes for chargeback accounting that allow valid chargebacks to fall through the cracks. Any administrator can keep track of one deal with one supplier. But when multiplied by thousands of suppliers and customers and hundreds of thousands of product agreement combinations, manual chargeback accounting is a liability. Inefficiency in the chargeback process has contributed to the steady decline in wholesale distributors' pretax profit margins across all sectors.

Imagine how much you can improve your profit margins by accurately tracking how much is sold to which customer over a specific period of time. You could accurately file all your chargeback claims – and do so in a timely fashion. You could say goodbye to lengthy dispute cycles, collect cash promptly, and re-deploy your staff in positions that add value to your company.

You can leverage information technology to turn this dream into a reality. By deploying an automated chargeback management solution, you can improve accounting and administrative productivity to facilitate the chargeback process. In turn, the increase in operational efficiency and profitability will drive responsiveness internally and across your supply chain.

## CHARGEBACK MECHANICS

In this era of heightened competition, manufacturers frequently offer special pricing to distributors to cover the cost of providing goods and services to customers, making it especially important for distributors like you to track chargebacks. These pricing arrangements serve a number of purposes. One common scenario occurs when a distributor is asked to provide products to customers at prices below the actual purchase price paid by the distributor. The distributor recoups the difference between its acquisition cost and the customer sales price through a chargeback – also known as earned income, deviated billing or sheltered income in the food service industry, ship and debit in high-tech distribution, and special price agreements (SPAs) in the electrical distribution industry.

Essentially, the chargeback process results in a rebate payment from a manufacturer to a distributor. Because wholesale distribution is a slim gross margin business, chargebacks are a critical source of income to ensure overall profit margins are maintained.

Here's how it works. A distributor sets up a proof-of-performance agreement with a manufacturer that entitles the distributor to a rebate once it has sold a certain number of units from that manufacturer. The rebate may be graduated, so the distributor receives one amount for 100 units sold and another amount for 1,000 units sold.

In addition, there are purchasing and selling chargebacks. With a purchasing chargeback, a distributor places an order with a supplier for 100 units of a product and receives a rebate for purchasing that quantity. But the distributor may earn another rebate when it sells the goods to the end user. Sometimes a portion of the rebate is passed along to end users for specific promotions.

The chargeback process may seem straightforward, but it can often be complicated and labor intensive to manage. Pricing agreements offer incentives at various levels of the supply chain. These incentives may be offered as warranty recoveries, marketing funds, and pricing-related credits. These arrangements are formalized in agreements that can span multiple customers, cover a vast array of products, and remain valid for several years. They can change frequently, and they can even be modified retroactively.

Keeping track of it all can be a real challenge. Wholesale distributors often wind up using a collection of inadequate tools, including spreadsheets, e-mail, faxes, and phone calls. The process is manually intensive and prone to error. As a result, distributors miss opportunities to file claims, or they become caught up in disputes and lengthy cycles of rejections and resubmissions that increase the days chargeback outstanding. Ultimately, this inefficient process drives up costs, impairs cash flow, and undermines profitability.

## THE CONSEQUENCE OF CHARGEBACK INEFFICIENCY

From executives to accounting clerks, your staff has a vested interest in ensuring records are accurate and cash is collected in a timely fashion. Yet inefficiency in chargeback processing limits effectiveness, ultimately undermining your overall financial performance.

C-level executives, for instance, are responsible for implementing strategies that maximize margins and cash flow. Without accurate information and a clear picture of the margin earned on products, executives can't plan effectively. And because unclaimed chargebacks could lead to cash crunches, executives may miss out on growth opportunities.

Sales vice presidents are responsible for increasing market share and operating margin, as well as optimizing incentive programs for sales representatives. Without accurate chargeback information, they can't obtain accurate margin and revenue reports or secure critical deals. And inaccurate information on the revenues generated by sales representatives prevents them from optimizing their commissions.

Financial vice presidents must ensure all valid claims are created while minimizing both the claim threshold values and the time spent on handling disputes. Often, agreements are not available in time to create claims, it's difficult to capture all the claim data, and manual processes require high claim thresholds. Disputes, when they arise, aren't resolved in a timely manner.

Commissions are the lifeblood of sales representatives, and they want to be certain that they receive the compensation that is due to them. But because they may not have access to the most current chargeback agreements, their commission records are likely to be inaccurate. That means sales professionals have to spend extra time clarifying terms so they aren't inadvertently short-changed in their paychecks.

Chargeback clerks ideally would like to close a larger number of claims on the first settlement run, reduce the overall claim settlement time, and increase their personal productivity. Instead, they are trapped by extensive manual processes, which increase the likelihood of error. They must access multiple systems – including some that are paper-based – to answer most questions. These staff members bear the brunt of chargeback inefficiency every workday.



## **TAKING THE COMPLEXITY OUT OF CHARGEBACK PROCESSING**

Chargeback data is reported to the manufacturer in several ways, although electronic transmission is the most common method. Data may be broken down by transaction or summarized. Both distributors and external agencies, such as group organizations or data providers, report chargeback data. Often, this data needs to be cleansed and validated before it is processed for payment.

For example, chargeback information needs to be validated against contract agreements to ensure authenticity. You need to verify whether the sale actually took place and if the price or quantity was modified. Accuracy is imperative, so that means checking to see if any line items were overlooked and all the pertinent information is complete. Clerks need to determine if duplicate claims were submitted or if a claim was resubmitted with the same information on another day. They also need to verify that the customer was eligible for the price, discount, or rebate; that claim amounts were consistent with the agreement; and that the customer did not return the product to the distributor or the manufacturer.

You can streamline these processes by deploying an integrated solution that supports electronic data interchange (EDI). The solution should contain all the functions needed to handle chargebacks systematically and efficiently. You should be able to create a variety of contract agreements with multiple manufacturers and end users, validate contract agreements, settle chargeback documents based on flexible parameters, reconcile and resolve disputes, produce reports, and establish a full audit trail for the entire chargeback life cycle.

Armed with an integrated solution, chargeback clerks can work more efficiently. Once they off-load manual processes, they have more time to focus on claims that require additional attention. Sales representatives no longer have to worry about applying the wrong pricing because they have access to the correct pricing information when and where they need it. In addition, sales vice presidents, financial vice presidents, and C-level executives have accurate information, so they can make better business decisions.

Technology helps to build trusted relationships with suppliers. Both parties understand disputes can occur, but when they do, you and your supplier have accurate data to resolve them on an exception basis. You can work together to optimize chargeback agreements for a particular customer, region, or product. You can also improve collaboration by making claim information available on a supplier portal.

Most important, greater efficiency leads to a positive impact on your bottom line and a quick return on investment. The reduction of unclaimed dollars directly affects your overall margin and improves your cash flow. Your dispute handling costs are lower, and you require fewer chargeback clerks.

## THE POWER OF EFFICIENCY: BORDER STATES

According to the National Association of Electrical Distributors (NAED), wholesalers can boost efficiency and profits by utilizing an integrated chargeback management solution and implementing the recommended best practices of the organization's SPA task force. One of its members, Border States, is already reaping the benefits.

Border States, one of the largest independent electrical distributors in the United States with branch locations in 11 states and Mexico, now spends 63% less time filing and reconciling SPA claims. Less time spent on chargeback processing translates into cost savings and greater efficiency, not only for the company, but also for the manufacturers whose products it sells.

The streamlined claims process has improved Border States' ability to track SPA claims from the time of end-customer invoice through the receipt of the manufacturer credit. The distributor receives credits much faster, and better coordination of data has allowed the distributor to forge closer relationships with manufacturers.

Before implementing the best practices, Border States spent about 175 staff hours each month filing and reconciling SPA claims. Today, that has dropped to 65 hours – a 63% reduction, and the company hopes to reduce it further to 45 hours a month. Border States now files 95% of its claims electronically over the new EDI-based system with 80% of those items receiving electronic replies from the vendor. As those proportions approach 100%, the time spent on SPAs will decrease even further. Reducing costs for the supplier and distributor ultimately reduces costs to end customers.



## A CHARGEBACK MANAGEMENT SOLUTION FROM SAP

SAP has developed an integrated application that helps companies collect and track all the revenue to which they are entitled. The SAP® Paybacks and Chargebacks application by Vistex is comprehensive, integrated software designed for wholesale distributors. With SAP Paybacks and Chargebacks, you can capture chargeback data, manage claims, control varied and changing chargeback agreements, and ultimately transform chargeback management into a systematic and effective process. The software allows you to manage the entire chargeback life cycle – from initiation to settlement – and to minimize manual intervention to bring new levels of efficiency and accuracy to the process.

SAP Paybacks and Chargebacks enables you to perform the following activities:

- Create and manage a variety of agreements with multiple suppliers and customers
- Apply evolving agreements on an ongoing basis to maximize chargeback recovery
- Automatically submit claims using flexible settlement parameters and calendars
- Communicate with partners via EDI or Web portal technology
- Park documents to give suppliers a broader opportunity to review and approve claims
- Handle interim settlements to accept approved amounts quickly without waiting for final resolution
- Produce timely reports and establish a full audit trail for chargeback activity to support corporate accounting and compliance efforts
- Use multiple currencies and units of measure in the chargeback process
- Monitor and reconcile outstanding chargeback claims using flexible search criteria
- Support a multitier distribution model in which initial ship-

- ments are received in consolidation centers and subsequently shipped to branch locations, and onward to end customers
- Use the reported chargeback data to control various performance programs, such as administration fees, market share rebates, and so on
- Aggregate chargeback document data in logistics information structures and provide extract structures for use in a data warehouse
- Provide a holistic overview of chargeback agreements with complete visibility at customer and product level using a checkbook approach

SAP Paybacks and Chargebacks is fully integrated in the mySAP™ ERP application. That means you can include documents from other enterprise processes, such as sales and procurement, in the chargeback process. And you can easily use chargeback information in your finance, controlling, and compensation processes. For example, chargeback recovery may affect incentive payouts to employees.

The complete integration of Vistex and SAP software also means there are no interfaces and up-front integration costs to manage; ongoing maintenance and upgrades are seamless. And because mySAP ERP is powered by the SAP NetWeaver® platform, you are assured of easy integration and flexibility in virtually any IT environment – all of which help ensure a low total cost of ownership.

## **SUMMARY**

You rely on chargebacks to protect your profit margin. But too often wholesale distributors give away this cushion simply because their manually intensive chargeback procedures are prone to error. You could simply hire more people to process chargebacks, but that would just increase your overhead.

Instead of struggling with manual processes, distributors should implement an automated chargeback management solution. This solution can streamline chargeback procedures and improve accuracy. Employees at all levels – from top executives down to chargeback clerks – can improve their job performance by having access to the right data at the right time.

For more information on how SAP Paybacks and Chargebacks can help you recover lost chargeback income, visit our Web site at [www.sap.com/usa/industries/wholesaledistribution](http://www.sap.com/usa/industries/wholesaledistribution).

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