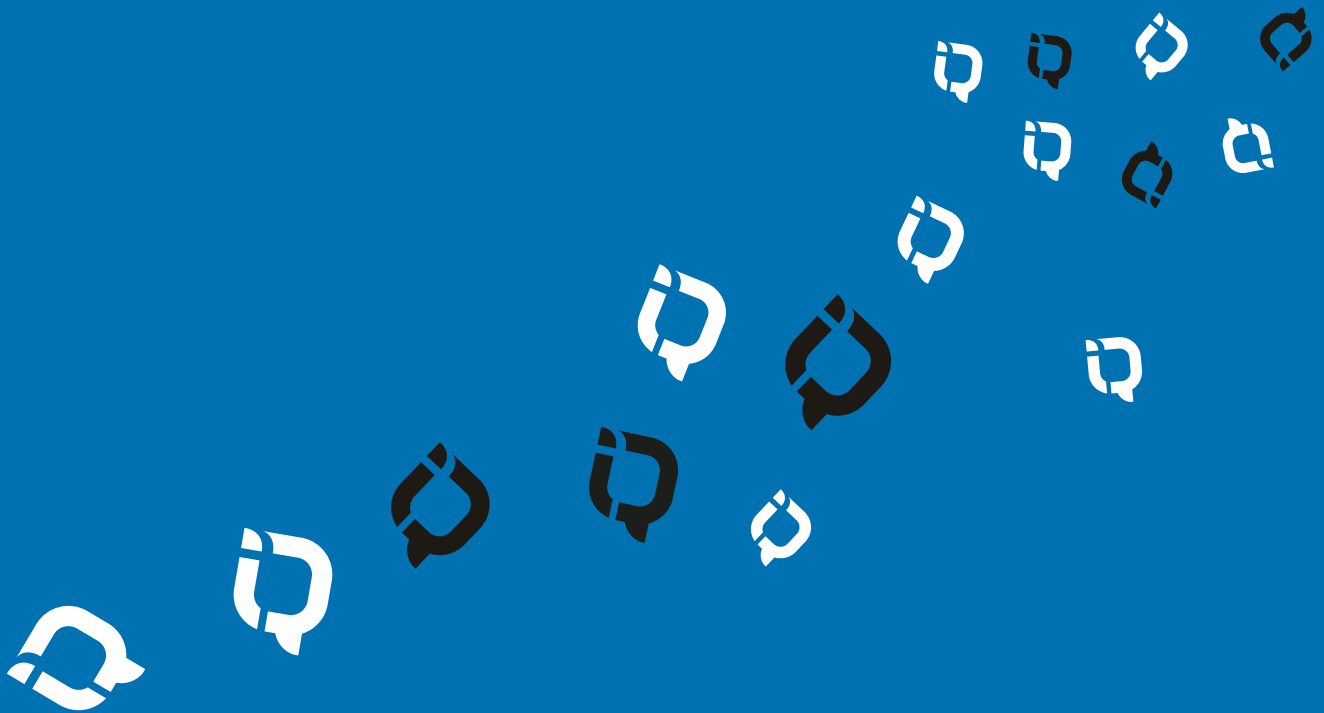




# Best Practices, Best Results

## The Importance of Best Practices in Accounts Payable





# Best Practices in Accounts Payable

Accounts payable is an expensive, error-prone process for many companies, but a focus on best practices can cut your costs by up to 68%, reduce error rates to less than 0.03% and build improved relationships between you and your vendors.

Depending on the industry, accounts payable is typically the largest or second largest disbursement of a firm's funds. Frequently, it's also the largest single cost and largest team in a firm's accounting department. On average, processing an invoice costs a company \$16.54, but even after investing that much, data entry error rates are still around 1.6%. These errors are compounded by the challenges of tracking, filing and auditing paper-based invoices. As a result, the business rules for invoice processing are often loosely documented and even more loosely followed, and many accounts payable managers spend more time fire-fighting than leading.

These challenges are significant, but each can be addressed by applying the following best practices to the accounts payable process:

- [Strengthen your accounts payable business rules](#)
- [Digitize your invoices and apply quality assurance](#)
- [Improve your accounts payable reporting and controls](#)
- [Consider outsourcing your accounts payable function](#)
- [Focus on continuous improvement](#)

## Strengthen Your Business Rules

Start by reviewing your rules for invoice processing and documenting how they are actually applied. This will give you real insight into how invoices are matched to purchase orders, how long it takes invoices to be approved and the amount of discretion each employee uses when handling exceptions. For a medium-sized company, a complete documentation of their accounts payable processes can run to 1,000 pages or more given all of the variations by vendor, location, type of expense, etc. The next step is to standardize your processes and ensure they meet industry standards. Each industry has its own standards, but common ones include:

- Refusing to pay an invoice that arrives without a previously issued purchase order
- Not paying until goods are received
- If an invoice triggers exceptions, a company may choose to short-pay the invoice and itemize the deductions to prevent vendor confusion
- Invoices that are improperly coded or cannot be matched are returned to the approver or buyer for correct coding

Implementing your new processes will generally require a combination of accounting systems, third-party solutions and proprietary software applications. Sophisticated accounts payable software can ensure your invoices are automatically matched against purchase orders, coded according to your business rules and forwarded to the appropriate managers for approval. Software of this quality also lets accounts payable staff log variances and exceptions in detail, for follow-up with managers and vendors.



You'll want to be sure the software integrates with leading payment systems and allows both you and your vendors to review the status of their invoices online, in real-time. Because they can quickly compare invoices across multiple fields of data, accounts payable software is also useful for detecting duplicate invoices. These commonly occur when a vendor sends a second bill after not being paid promptly. Unless they're caught, duplicate invoices frequently result in overpayments that are time-consuming to recover.

### Digitized Invoices and Quality Assurance

Even the most fully supported workflows can go awry if a paper invoice is damaged or lost. Every time a piece of paper is handled, from opening an envelope to leaving it on a desk to putting it in interoffice mail, there is an opportunity for that piece of paper to go missing. These opportunities multiply if a business gathers invoices from multiple locations for centralized processing or if multiple managers need to approve an invoice. On top of that, a simple filing error can make paper documents difficult, if not impossible, to locate.

Even if it isn't lost, a paper invoice can sit in a manager's inbox for days or even weeks while the manager handles more pressing issues, avoids incurring a cost or simply forgets the invoice is there. These invoices represent lurking liabilities whose amounts and due dates are unknown. In a real sense, they are time bombs waiting to go off against a company's balance sheets. Failing to pay invoices in a timely manner also leads to poor credit from vendors, who may apply late charges or deny discounts.

To alleviate these problems, all invoices should be received and logged in a central location, and companies should insist on receiving electronic invoices when possible. Electronic invoices are delivered in EDI, XML or other formats, and then matched against purchase orders in software-based accounting systems. They not only reduce data entry and error rates, but increase processing speed as well. Note that none of this applies to PDFs of invoices, which are worse than paper invoices because the PDFs still need to be printed and loaded into your system. In addition, PDF invoices have a higher rate of duplicates because they are so easy for a vendor to send. Any remaining paper invoices should be scanned into the system, corrected as necessary and reviewed by a separate member of the accounts payable team. This combination of software, human correction and quality review reduces error rates to as low as 0.03%.

Some companies have implemented optical character recognition (OCR) software, but it only has a 99.5% accuracy rate, which means one in every 200 characters will be wrong. This could be a field that is unimportant or could be the amount field. This makes OCR a dangerous proposition unless you can devote the resources to double-checking each invoice.

Logging invoices helps your accounting staff maintain a true picture of a company's liabilities. With an electronic workflow system, invoice images can be routed electronically for approval and managers can be reminded to approve or reject all invoices within two days of their receipt. By encouraging prompt issue resolution and payments, an electronic



workflow system can help a company qualify for early payment discounts.

### Improve Controls and Reporting

The accounts payable software you select should offer web-based reporting and drill-down tools without per user fees. These web-based reports should be easy to use, and include:

- Drill-down reports that display the transaction and associated source document image
- Real-time reports of the invoice's approval and payment status
- Monthly liability reports
- Customized expense reporting
- Exception reporting
- Auditing reports
- Time and expense reports for invoice processing

### Outsourcing

Accounts payable is a transaction processing function, not an accounting function. This means that accounts payable requires more management time and employee supervision, more technology and more capital than other financial processes. It also means more "fire-fighting" when errors occur. The techniques required to manage accounts payable successfully differ markedly from those required to manage accounting functions and also require more management training.

One way to surmount these challenges is to outsource accounts payable processes to companies who can handle these non-core business functions

more efficiently and effectively than you can internally. Not only do such companies frequently offer significant savings over in-house processing costs, but they also offer quality oversight, improved controls and auditing programs that can increase accuracy to as much as 99.97%.

An established outsourcing company can help guide a complete and objective review of your business processes, and ensure they comply with industry standards. An outsourcer can also draw on its experience to implement electronic invoicing across a variety of vendors and to apply rigorous quality oversight to your accounts payable programs.

By transitioning your accounts payable function to an outsourcing company, you can redirect staff, management and financial resources to focus value-generating activities that support your core business.

### Continuous Improvement

Implementing the best practices described above is only the beginning. To sustain a performance advantage, a company needs to focus on continuous improvement. This starts with gathering pertinent performance data and analyzing it for opportunities to improve efficiency. It includes studying ongoing issues to determine their root causes and eliminate them. For example, if reports show that one vendor is responsible for a disproportionate number of exceptions, this creates an opportunity to work with that vendor to develop better invoicing. Over the long term, this will result in a better understanding and a tighter relationship between the two companies.



Continuous improvement also means not standing still technologically. As new tools and services are introduced to the marketplace, they need to be considered and, as appropriate, adopted.

## Sarbanes-Oxley Compliance

A concerted focus on best practices in quality, controls, reporting and continuous improvement will make it easier for your company to achieve Sarbanes-Oxley Section 404 compliance. Section 404 requires a company's management to acknowledge its responsibility for the company's internal control structure and its procedures for financial reporting, and also assess the effectiveness of these structures and controls. In a company's quarterly reports, management must evaluate the impact that material changes to the company's internal controls have on their effectiveness. In a company's annual reports, an independent auditor must attest to management's statements. Following best practices make it easier for auditors to review a company's controls and confirm its Section 404 compliance.

### About IQ BackOffice

IQ BackOffice provides high-quality, low-cost accounting and human resources solutions to clients of all sizes. By combining accounting expertise, operational excellence and innovative technology, we bring manufacturing-grade standards to your back office processes and integrate your billing and payment systems with your vendors and customers.

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## Summary and Benefits

An accounts payable system dedicated to best practices will:

- Document and standardize all invoice matching and approval business rules
- Utilize well-documented business rules around coding
- Utilize workflows to electronically route invoices for approval
- Implement quality oversight on data entry and coding functions
- Audit the application of business rules and workflows
- Integrate an imaging system into the accounting system
- Centralize receipt of invoices at a central location
- Implement workflows through a combination of accounting systems, third-party and proprietary software solutions
- Offer real-time reporting on financial liabilities, exceptions, invoice status, cycle times and costs
- Seek opportunities for continuous improvement
- Make it easier to comply with Sarbanes-Oxley requirements

A committed focus on applying best practices will reduce the cost of invoice processing and the error rates associated with it. Companies can reduce the error rates associated with their accounts payable invoice processing from 1.6% to less than 0.03%. They can also reduce their per-invoice processing costs up to 68%.

