

Accounts Payable

**How to cut costs
and improve invoice
processing efficiency**

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Introduction

If you haven't already, it's time to formulate and execute a strategy to automate invoice processing. The direct and indirect costs of traditional manual processing are just not necessary.

The technology to eliminate the great majority of the paper handling is available, affordable, and easily implemented within the context of your existing financial systems. And the benefits go beyond cost reduction to creating a cost management and information availability advantage that will help your company better compete for years to come.

Just keep in mind that automated invoice processing is about more than just scanning invoices into a document management system or capturing invoices electronically. To get the results you're really after, you want to automate the full invoice life-cycle from the time they are received to the time they are authorized for payment.

Yes, like most important initiatives, effective invoice automation will require some level of policy and procedure development, and may require some manageable organizational changes before technology can be effectively deployed.

But once you have the foundation in place you can steadily automate more and more of your invoices until you are:

- ① No longer handling much paper at all.
- ② Properly paying a high percentage of invoices without the need for any human intervention.
- ③ Collecting the information you need for greater control of cash, clearer visibility of spend, and better management of budgets.

At a minimum, the results will be:

- ① Significantly reduced transaction costs.
- ② Increased payment terms discounts.
- ③ Improved supplier interaction leading to better future contracts.

This guide is intended to provide you with:

- ① A more detailed understanding of the challenges associated with invoice processing.
- ② An outline of the goals you should realistically have for invoice processing automation.
- ③ A clear picture of what invoice processing automation looks like.
- ④ A practical step-by-step approach to achieving a high level of invoice automation.

The challenge of invoices

In many organizations, invoice processing is the single most paper-intensive, "high touch" manual activity. Even organizations that have largely automated their front office, operational and supply chain functions often still process invoices manually.

Challenges of Accounts Payable

The problem starts with the fact that invoices are often not sent to the Accounts Payable (AP) department. They are frequently sent to the person who purchased the product or service and may sit on that person's desk for days or even weeks. Then there's more time and effort forwarding the invoice to AP before it can be entered into the accounting system. Sometimes departmental procedures are methodical, but create even more paper.

But plenty of challenges exist within the AP department as well. Whether received directly from the supplier or forwarded from elsewhere in the organization, invoice processing is very labor intensive. Besides the obvious mail handling and data entry activity, invoices must somehow be coded with appropriate purchase categories and GL accounts. That alone may require a lot of time-consuming research by AP personnel. In order to make sure the charges are valid, invoices need to be compared to one or more POs or a contract, and receipt of the goods or service needs to be confirmed. If the information isn't available or the invoice doesn't match the information AP has access to, the invoice needs to be sent to an appropriate person for review and approval. That takes more time. The more this is done with paper, the more time it takes and the more cost it accumulates.

There is no question that paper invoice handling is the enemy of efficiency in the AP department. Scanning invoices into a document management system can help, but by no means solves the entire problem. Receiving invoices electronically helps more, but only if the rest of the process is set up to automatically use the information.

Manual invoice processing results in a number of problems:

- ④ Management does not have visibility of outstanding liabilities.
- ④ Invoices are beyond the discount period before they even enter the AP system.
- ④ The potential for paying duplicate invoices increases as suppliers send second copies.
- ④ The inclination to "just pay it" becomes greater when the validation process is complex.
- ④ AP personnel end up spending time answering inquiries from suppliers about payment status.
- ④ Suppliers may stop delivering inventory or services when invoices are not paid on time.
- ④ Audits become long, costly and problematic.

And that is all in addition to the direct cost of invoice processing – primarily Accounts Payable personnel and departmental operating costs. Industry analysts suggest that on average, it costs bottom performing companies ten times more to process an invoice than top performing companies.

That means the difference between bottom and top performers can be over \$30 per invoice! Multiply that by thousands of invoices, add the cost of missed opportunities for early payment discounts, and add the cost of AP FTEs, and it's easy to see that the direct cost of inefficient invoice processing is substantial.

The goals of invoice automation

You may well pay for your investment in invoice processing automation just by reducing the direct cost of invoice handling. But you should set your sights on a number of other goals as well.



The benefits of fast, accurate, "low touch" invoice processing are actually far-reaching. To realize the full benefit, you should consciously set the following objectives:

- ④ **Reduce direct invoice processing costs** by improving efficiencies and cycle times.
- ④ **Ensure proper payment** and avoid fraud by improving controls and audit trails.
- ④ **Reduce overall purchase costs** by leveraging early payment discount opportunities and avoiding late charges.
- ④ **Improve working capital management** with greater visibility of payment liabilities and invoice status.
- ④ **Improve budget management** with better visibility of commitments.

- ④ **Improve procurement effectiveness** with better information for spend analysis.
- ④ **Strengthen supplier relationships** with better communication and on-time payment performance.

Even though the word "automation" certainly implies the use of technology, you should recognize that technology is not the be-all-and-end-all of your automation initiative – it is just an enabler.

The key to successful invoice processing automation lies in the re-design of management processes and a clear strategy for leveraging the available technology to meet the business goals listed above.

Companies that rely on traditional invoicing, payment and financing practices, which are burdened by many inefficient, manual tasks, will find themselves at a competitive disadvantage to companies that have automated this process.

Automated companies can better manage their spend and vendor relations at all levels.

The key elements of invoice automation

So what does invoice processing automation actually look like? Where does it start, and where does it end? What are the detail steps to be automated?



The basic concept is simple – that is to process all invoices in a common, electronic manner, enabling as many invoices as possible to be processed “straight through” with little or no need for human intervention, and to make the communication required for exception handling as fast and clear as possible.

The main elements of automation are:

Invoice capture

The first step is to turn all invoices received into a standardized electronic record for use in all of the other automation steps. If necessary, paper invoices can be manually keyed, though that process can be streamlined with readily available document scanning and OCR technology. Electronic invoices from trading networks, a supplier portal, and other supporting systems need only be translated into your standard format.

Realistically, you will probably use several different methods of invoice capture, with the goal of reducing the percentage that need to be manually entered over time. But one note: contrary to what some people think, streamlining invoice capture does not represent nearly the savings opportunity as streamlining the way you process them once you have them captured does. Scanning and invoicing are only preparatory steps and do little on their own to reduce costs. Automation of the following steps is where the real savings lie.

Invoice validation and coding

This step can be very time and resource-consuming when processing invoices manually. It can also be prone to frequent errors that distort financial and procurement information over time. In an automated process, the system should be able to use invoice information such as the vendor ID, PO#, contract ID, item codes, etc. to automatically determine purchase categories and GL accounts. More sophisticated systems

can even “learn” how to code invoices over time to continuously reduce the amount of human interaction that’s needed. For instance, it can “learn” what departments to be charged based on phone numbers in a complex telecom bill.

In an automated system, this step should also highlight obvious and not-so-obvious duplicate invoices.

Invoice matching and automatic approval

Again, this can be a big job when processing invoices manually. And it’s a step that may be skipped when Accounts Payable staff are particularly pressed for time or don’t have ready access to the right information. In an automated process, PO-based invoices can be electronically compared to PO and receipt records from your purchasing system. Non-PO invoices can often be compared to contracts. Invoices that match can be automatically approved for payment.

Of course invoice details like freight charges and taxes can make this more difficult than it sounds on the surface, but a good system will provide sophisticated logic and user-set tolerance ranges that enable a very high percentage of valid invoices to be automatically approved.

Discrepancy resolution and approval

There will always be some invoices that are questionable or need a particular manager’s approval. Even with automated matching, there will still be the need to route a certain number of invoices for review, possible supplier dispute and eventual adjustment or approval.

The key technology here is electronic workflow. An automated process will enable Accounts Payable personnel to quickly route invoices to appropriate people via email. In many cases, the system will even automate that. Unlike sending paper, the invoice and all associated information

will be instantly available to the reviewer. Simple approvals can usually be done with a single click. The whole cycle may only take a few minutes or hours, rather than days or weeks.

Payment authorization

Once invoices are approved for payment in an automated system, they are passed directly to the financial system for payment scheduling based on the usual factors such as due date and discount date. The good news is that they get to that point far sooner than they typically do with manual invoice processing. That means cash management policies can be exercised as desired and savings from available discounts can be realized. This also eliminates errors that can potentially be introduced by re-keying.

Supplier communication

In an automated system, the status of invoices is always known and accessible electronically. That makes it possible to give suppliers self-service inquiry capabilities via a secure supplier portal. Not only does this significantly reduce the enquiry-handling load on the Accounts Payable department, it also gives suppliers piece of mind and the feeling that your organization is "easy to do business with". That and the time you save them when they don't need to chase late payments may well come into play when future purchases or contracts are negotiated.

Don't under-estimate the percentage points that can be shaved from your overall purchase costs over time.

Reporting and analysis

Last but not least, an automated invoice processing system enables all kinds of reporting and analysis that is simply not possible when invoices are handled manually. Invoices are electronically captured, validated and coded. Because it's done sooner, Financial Managers

have much better visibility of near-term cash requirements, enabling better management of working capital. Because it's done more thoroughly and accurately, Procurement teams have better information for spend analysis, contract negotiations, and supplier relationship management.

In addition to these main elements of automation, there are a few important underlying attributes that are essential to making your invoice processing system effective:

A highly flexible filing system

Invoice records and associated information such as scanned documents will need to be viewed and processed in many different ways throughout their life-cycle. The ability to look up, organize, sort and filter this information according to the criteria that is important to your organization is key to overall productivity.

An open architecture

In order to introduce the type of "invoice processing engine" described above without the need to replace existing financial and purchasing systems, the software needs to be designed in a way that enables it to easily access or import information from your existing systems.

An intuitive user interface

Even though some of the inner workings of your invoice automation may be quite sophisticated, the system needs to be easy to understand and use by your AP personnel and others. For instance, 3-way matching may involve as many as 20-30 different tests. The system needs to make discrepancies easy to interpret and should provide the ability to take appropriate action with just a click or two. An intuitive user interface design is key to the productivity of individuals.

A step-by-step approach

So how do you go about getting from where you are today to effective invoice processing automation? Fortunately, this is one important initiative that can be undertaken as a series of small steps, and can generally be done without making any significant changes to your existing systems.

Initial steps don't require new systems at all in order to deliver incremental benefits. Technology only comes into play once a foundation of policies and procedures are established. Consider the following steps:

Analyze current processes

Find out how invoices flow through your company today. Where are they received? How do they get to Accounts Payable? How are they validated and coded? What percentage is received electronically vs. in paper form? What is the average time it takes to process an invoice? How many invoices are processed per year per AP FTE? What is the AP cost per transaction (total invoices / AP department cost is at least a rough measure).

Your goal is to understand how you process invoices today, where bottlenecks and delays exist, and how much it's costing. You will probably find opportunities to improve your current procedures, even in the short term.

Centralize invoice management

Consider establishing a centralized or shared service for invoice management. Inform your suppliers that they should send all invoices to your Accounts Payable function and enforce the policy. (In a survey done by the International Accounts Payable Professionals association (IAPP), more than two thirds (64.7%) of members stated centralization was of utmost importance by giving it an importance rating of 5 on a scale of 1 to 5).

Implement a standard approach that captures invoices into some type of electronic form. You may start with a simple document scanning and indexing process. If you need to capture invoices in multiple locations, use a standard approach and centralized electronic filing system that will

streamline your manual approval process.

Your primary goal at this point is to capture invoices as soon as possible and to position yourself for later automation.

Standardize policies and procedures

Define and document standard policies and procedures for processing of PO and non-PO invoices – e.g. duplicity and mathematical integrity checks, matching criteria and tolerances, discrepancy resolution workflow, dispute and approval workflow, etc. Also document your policies for working capital optimization – e.g. when to take and not take early payment discounts.

Your primary goal is to clarify to your organization exactly how invoices should be processed. This will better guide your current manual processes and prepare you for automation of your policies and procedures.

Automate

Once you have established your policies, procedures and controls, you are ready to begin automating. At that point you are ready to select and implement a technology solution that provides the elements of automation described in the previous section.

The most important thing to first put in place is a single "processing engine" that will enable you to automate your policies and procedures for validation and coding, matching, discrepancy resolution, payment authorization, and reporting and analysis. You want a single, consistent invoice automation process regardless of how many ways you initially capture invoices. On the front end, you can leverage any electronic invoicing opportunities

you may already have in place whilst using a combination of scanning, OCR and keying to capture paper invoices.

Your goal is to process as many invoices as possible "straight-through" with little or no human interaction, and to significantly streamline the discrepancy resolution process. Once that capability is in place, you can work on incrementally improving the front-end capture process. We will discuss that more a little later.

Enable supplier self-service

With all invoices being processed in a consistent electronic manner, it's an easy step to make status information available to suppliers via a secure self-service internet portal. Your goal here is to eliminate the time AP personnel currently spend on the phone answering supplier questions about where their invoice stands and when they will get paid.

Proactively request early payment discounts

With the ability to process invoices much more quickly, you will be in a position to take advantage of any early payment discount terms your suppliers may offer. In addition to current opportunities, you may want to begin asking for such discount terms as you negotiate new contracts. Once you have a real handle on invoice processing, this may be a source of significant savings over time.

Leverage information for better sourcing

Invoice processing automation can help your Procurement department enhance their sourcing activities in a couple of ways. First, with all your payment activity electronically captured, they will have better information for spend analysis for purposes of supplier base consolidation and other

activities sourcing. Second, with a reputation for paying on time and making it easy for suppliers to manage their accounts receivables with you, suppliers may be more willing to give your organizational preferential prices and terms.

Your ultimate goal here is to provide your procurement people with information and on-time payment performance that enables them to gain even better value from suppliers over time.

Incrementally automate invoice capture

As soon as you have your back-end invoice processing automated you can turn your attention to finding even more efficient ways to capture invoices on the front end. This can be done on an incremental basis by implementing electronic invoices with your larger customers or through trading networks, and/or by adding capabilities like invoice upload or "PO Flip" to your supplier portal. All of these methods will act as increasingly efficient means of moving invoices into automated invoice processing.

Your goal here is to continue to take cost and time out of invoice capture – even after you've achieved the big savings from automated invoice processing.

Each of these steps is manageable and provides incremental benefits. As stated at the beginning of this guide, the direct and indirect costs of traditional manual processing are just not necessary anymore. The technology to eliminate the great majority of the paper handling is available, affordable and easily implemented within the context of your existing financial systems. And the benefits go beyond cost reduction to creating a cost management and information availability advantage that will help your company better compete for years to come.

Let's talk

Regardless of where you are on the AP journey, we're always open to discussing your objectives and how we can help.

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