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From the Shadows to the Forefront

AP Automation and the Strategic Vision

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From the Shadows to the Forefront: AP Automation and the Strategic Vision

The payments department is essentially the custodian of an organization when it comes to cash flow, which in turn is the lifeline of liquidity. If either one of the two core functions — Accounts Payable (AP) or Accounts Receivables (AR) — within the payables realm is inefficient, effectively an organization's ability to accurately forecast its financial position is also compromised. Financial forecasting is a fundamental strategic function and often garners attention from the office of the CFO, yet somehow AP has lurked in the back-office shadow and is considered a tier two function when it comes to capability assessment and investments.

This analyst insight, based on survey responses of over 100 financial services executives actively involved in the payments space, bridges the gap between AP automation and strategic vision. We will discuss some of the key market pressures which compel organizations to refine their AP processes and will also identify key technological capabilities which enable Best-in-Class companies to out-perform their peers across the following key metrics:

- Invoice processing cost: Best-in-Class process their invoices at 0.17 of the cost as reported by Laggards.
- Time to process an invoice: Laggards take 3.86 times as long as Best-in-Class companies to process an invoice.
- Early payment discount capture rate: Best-in-Class companies are 7.4 times as likely as Laggards to capture early payment discounts.

This study will conclude with a discussion of the impact of AP optimization on the bottom-line and make a case for AP's role in attainment of strategic goals.

Need for Efficiency Driving AP Initiatives

According to the May 2012 report, *AP Invoice Management in a Networked Economy*, difficulty finding or managing paper-based documents was cited as the third most pressing concern by 39% of the respondents, while lack of visibility into invoices and AP documents led the pack with 45% of respondents selecting it as the top-most market pressure. This year's findings report a minor order shift but the overall concerns remain the same.

Difficulty finding or managing paper documents emerges as the leading market pressure, cited by 36% of the respondents, and lack of timely response either in terms of reconciling accounts or addressing exceptions tie for the second place at 35% (Figure 1).

Analyst Insight

Aberdeen's Insights provide the analyst's perspective on the research as drawn from an aggregated view of research surveys, interviews, and data analysis.

Aberdeen Methodology

The Aberdeen maturity class is comprised of three groups of survey respondents. Classified by their self-reported performance across several key metrics, each respondent falls into one of three categories:

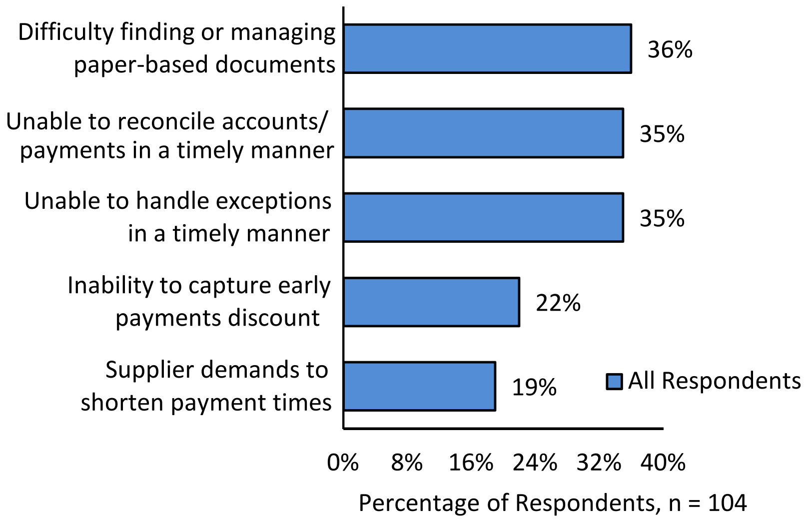
√ **Best-in-Class:** Top 20% of respondents based on performance

√ **Industry Average:** Middle 50% of respondents based on performance

√ **Laggard:** Bottom 30% of respondents based on performance

Sometimes we refer to a fourth category, **All Others,** which is Industry Average and Laggard combined.

Figure 1: 'Find and Address' — Key Market Drivers



Source: Aberdeen Group, September 2013

Paper-based documents are cumbersome and difficult to track. It can be an onerous task to not only keep a paper trail but also to find a relevant document in a timely manner. Some vendors may submit a Purchase Order (PO), a contract, or maybe an invoice and some might submit all three documents per order. Navigating through these and additional documents can be a time-consuming task. Further, one missing document cannot only hinder financial transparency, but can also lead to frustration on both the buyer's and supplier's part, leading to a severed customer relationship. Therefore, management of paper-based invoices still remains a top concern for the AP department and is closely tied to an organization's overall financial management process. According to the August 2013 Financial Transformation for Operational Excellence survey, 31% of the respondents cite the need to manage the growing volume of transactions as a key market driver to improve their financial management processes.

On the same note, inability to reconcile accounts and payments, or to handle exceptions in a timely manner, reflects poorly on an organization's ability to address customer concerns and offer quality service. Inability to reconcile accounts and payments in a timely manner has a direct adverse impact on financial reporting accuracy and forecasting. Case in point, as per the Financial Transformation survey, 62% of the respondents cite the need for expedited financial information delivery but if the very lifeline of cash flow — accounts payable — is unable to offer an accurate picture of the financial position, then how can companies forecast and officiate their strategic initiatives? If accounts payable ever wants to be viewed as a strategic function, then it must address this tactical issue first.

On the bright side, it is heartening to note that all of these market drivers are becoming less of a concern (note the drop in percentage, from 45% for the leading market driver in 2012 to 36% for the current market driver) as

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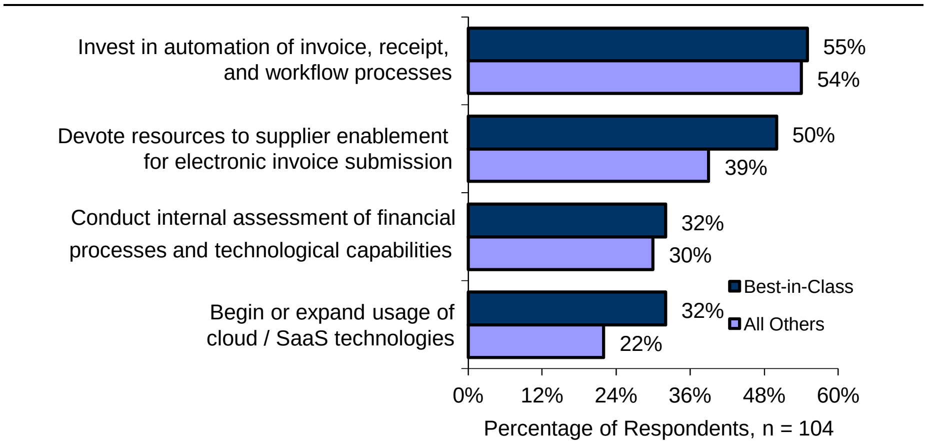
the AP industry continues to mature and more organizations embrace automation. In fact, the playing field is leveling off quite well — Best-in-Class and All Others report similar statistics with regards to investment in automation of their Invoice, Receipt, and Workflow (IR&W) processes (Figure 2).

Still, Best-in-Class companies report a competitive edge over their peers as they continue to refine existing AP processes incrementally improving along the way. Continuous improvement is really at the core of the Best-in-Class strategies, a few of which are discussed in the following section.

Best-in-Class Companies Go Beyond Automation

All Others are closing in on the Best-in-Class companies with regards to the IR&W automation rate (Figure 2) and are in line with industry trends around mature business functions and lines-of-business (LOB). It really is a dual effect — on the one hand as more solution providers enter the industry, the price-point tends to drop and as businesses continue to expand or even streamline existing initiatives, it becomes more price-effective and scalable to automate certain core processes.

Figure 2: Enable, Assess, and Expand — Strategic Refinement



Source: Aberdeen Group, September 2013

Let's assume that everyone invests in solution A and embraces the automation route. Then how does one emerge ahead of the pack? The answer is enhancements through complimentary solutions. According to Figure 2, Best-in-Class companies are 1.28 times as likely as their peers (50% for the Best-in-Class versus 39% for All Others) to devote resources to supplier enablement for electronic invoice submission. This is no ordinary task as most suppliers have minimal or no incentive for submitting invoices electronically when they can continue to mail in or fax paper-based invoices. The onus of this initiative and its subsequent success really lies on the AP department on the buyer's side. They not only need to educate suppliers on the benefits of electronic submission but must also allocate their own resources to help with the installation and training in some cases of an

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electronic portal. It might seem like extra work for AP departments, but the benefits in terms of managing documents and financial transparency in due course outweigh the upfront heavy lifting.

Another area where Best-in-Class companies lead the pack is in terms of usage of cloud or SaaS-based technologies (32% for the Best-in-Class versus 22% for All Others). Best-in-Class companies are not only able to meet the needs of growing business, as they expand to different regions, but also enable their AP department to monitor payables at their convenience.

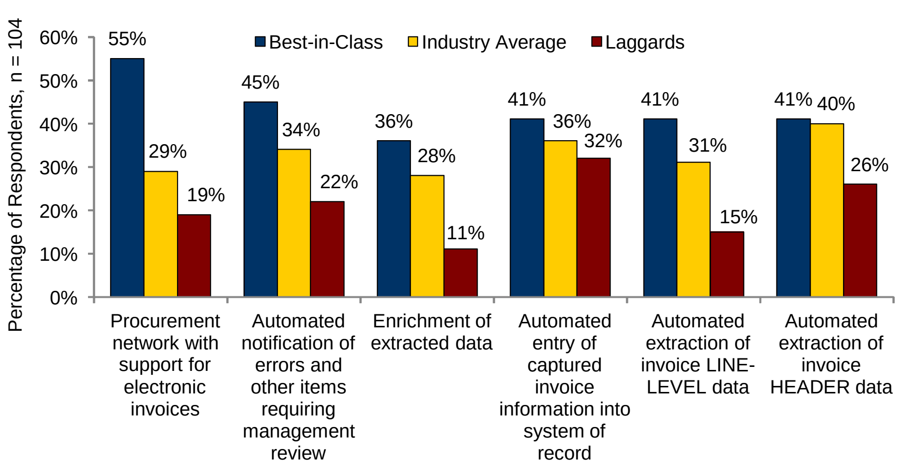
Benefits of these strategies in conjunction with key capabilities help Best-in-Class companies achieve superior performance compared to their counterparts (please refer to the sidebar). The following section explores some of the key capabilities which the leading companies use to further refine their existing strategies.

Attention to Detail: The Best-in-Class Capability Mantra

According to the Financial Transformation survey, 39% of the respondents consider the level of challenge across the Procure-to-Pay (P2P) workflow between medium to high. Best-in-Class companies rated it at 1.0 (on a scale of 0-to-3, where "0" indicates "no challenge" and a "3" indicates "high challenge"). The Industry Average and Laggards rated it at 1.3 and 1.5, respectively, indicating low-to-medium challenge.

One of the reasons that the Best-in-Class have been able to streamline their P2P workflow is by investing in technological capabilities to support their procurement network. Best-in-Class companies are 189.5% more likely than Laggards (55% for the Best-in-Class versus 19% for the Laggards) to offer support for electronic invoice across their procurement networks (Figure 3). Consequently, they help both suppliers and buyers get on-board with electronic invoice management and expediting the workflow by automating sub-processes across the entire chain.

Figure 3: Best-in-Class Focus on Details



Best-in-Class: Accounts Payable Reporting Criteria

Respondents to the 2013 E-Payables: Payments Automation for Operational Excellence survey were ranked on the following criteria:

√ **Invoice Processing Time (Days):**
Best-in-Class – 3.7 days, Industry Average – 8.8 days, Laggard – 14.3 days

√ **Invoice Processing Cost ($US):**
Best-in-Class – $4.0, Industry Average – $9.6, Laggard – $23.3

√ **Early Payment Discount Capture Rate (%):**
Best-in-Class – 65.8%, Industry Average – 42.7%, Laggard – 8.9%

Source: Aberdeen Group, September 2013

Best-in-Class companies focus on details and enhance existing capabilities, either through the automation of intermediate steps such as notification of errors, invoice information systems entry, data extraction — at both line and header level, or through data enrichment to capture vital information across unstructured data.

All of these positively impact both the P2P and the purchase-to-pay processes in terms of reduction in invoice-processing time. Laggards take 3.86 times as long as the Best-in-Class to process an invoice (3.7 days for the Best-in-Class versus 14.3 for the Laggards; sidebar on page 4). Besides the quantitative benefit, Best-in-Class companies also pave the way for better customer relationships. For instance, by enriching existing data and capturing critical information across unstructured data, Best-in-Class companies gain valuable insight on their buyers and can tailor solutions to meet their credit needs and detect non-payment risk. The Best-in-Class are 227% (36% for the Best-in-Class versus 11% for the Laggards) more likely than Laggards to enrich existing data.

Similarly, by automating exception notification, the Best-in-Class are expediting the review process and enabling dispute resolution in a timely manner, once again better understanding their customer and enhancing the overall customer experience. Best-in-Class companies are over two times as likely as Laggards (45% for the Best-in-Class versus 22% for the Laggards) to automate error notification. According to the Financial Transformation survey, only 9% of the Best-in-Class companies cited an inability to handle invoices in a timely manner compared to 16% of All Others.

The question remains — how can these capabilities and strategies help with an organization's strategic vision and why should the office of the CFO care? The following section connects the dots by showcasing the impact of AP automation on an organization's bottom-line.

Case Study: Financial Advisor Firm Embraces AP Automation

Throughout the course of his career, the Director of Accounting at a Sunnyvale, California-based, publicly traded, financial services firm has been involved in technology projects around accounting and process automation. This experience includes seven accounting and two customer relationship management (CRM) system implementations and he is currently overseeing the accounting system conversion to a cloud computing system.

According to the director, the payable digitization process has been challenging. "A comparison between Accounts Payable (AP) and Accounts Receivable (AR) is informative. As far as AR is concerned, digitization happened nearly overnight. 94% of our customer invoices are uploaded using a CSV file. We then provide CSV output to large partners and issue PDFs to customers that receive one to 12 invoices per year. When we were undertaking digitization, only one customer opposed it;

Case Study: Financial Advisor Firm Embraces AP Automation

everyone else supported it. That one customer gave in several months later!" notes the Director.

Additionally, the director notes that his current organization has multiple vendors. Of those vendors, 10 to 20 have multiple bills per month and three to four vendors issue anywhere between 60 to 100 bills per month. These key vendors are "business partners" who quickly agreed to provide CSV input that can be uploaded to their accounting system. The rest of the vendors tend to be small-to-medium-sized, privately held companies that continue to rely on paper invoices. "These smaller companies may not have an internal champion driving AR digitization," shares the director.

According to him, AP's digital evolution is even more challenging across small companies. It is not uncommon for a small-sized business to send one paper bill per month. This poses a challenge in terms of time and effort for the customer. "People solve problems with the tools they know how to use. Thus if someone doesn't know of the possibilities, then they don't know what they might do," states the director.

"People can be resistant to change and can have difficulty embracing new technology adoption. Adoption is the real challenge, when it comes to AP automation."

When asked about the preferred deployment method, he states that standard AP processes are quite basic in functionality and do not vary significantly from one company to another company. All AP departments have expense reports to process, may or may not employ a purchase order, they receive vendor bills from external sources, process approvals, write checks, final match, and file. Consequently, AP can use an off-the-shelf solution with small-to-moderate customization.

The Director of Accounting has been very pleased with the improvement in their current processes both in terms of operational efficiency and monetary benefit. "We digitized expense reports and POs with workflow years ago. We implemented vendor bill workflow in the past year. Prior to this recent change, it took much longer to process a payment. On average, we would be late by about five days. However, since implementing vendor bill workflow, we pay on average five days before the payment is due. So we're now saving 10 days.

"Bills took anywhere from a week to 10 days for approval. Now it takes on average two and a quarter days for approval and in some cases less than an hour. Lastly, we eliminated filing cabinets and off-site archiving," adds the director.

When asked about the emerging trends in the AP space and what advice would he give to those considering AP automation, the Director of Accounting has some very clear objectives — both for his organization

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Case Study: Financial Advisor Firm Embraces AP Automation

and the payments landscape as a whole. "Our conceptual design for AP is heading in the right direction, with a strong focus on execution and payment. With good systems you can measure all sub-processes. Our next big focus is improving the timing of purchase-order filing. Additionally, we are trying to take advantage of the automation facility on our banking website with positive pay, and online wire, and ACH approvals. We are hoping to eliminate most checks with ACH payment."

However, as with any new technology initiative, executive support is critical to optimize return on investment and to encourage adoption. The director expresses the need for senior executive sponsorship and remains very optimistic about the future of payables. "If process efficiency is exciting to you, then this is a very fun time to work in payables automation," concludes the director.

Source: Aberdeen Group, September 2013

Conclusion: Connecting AP Automation to the Strategic Vision

We've thus far presented capabilities and strategies which help Best-in-Class companies outperform their peers across AP management. But the story doesn't end here. In fact, if anything, it only begins as the impact of an efficient and a streamlined AP is permeated through the organization and has a direct impact on the organization's bottom line.

Accounts payable departments across Best-in-Class companies have superior operational forecasting capabilities than their counterparts. Table 1 clearly showcases the level of accuracy between actual and target Days Payable Outstanding (DPO) across all three categories.

Table 1: Actual versus Target DPO

Days Payable Outstanding (DPO)	Best-in-Class (Days)	Industry Average (Days)	Laggards (days)
Actual	21	33	34
Target	21	28	29

Source: Aberdeen Group, September 2013

This directly translates into greater financial reporting accuracy at an organizational level. Best-in-Class companies report 96.1% financial reporting accuracy over the last 12 months, compared to 87.9% for Industry

Average and Laggards. Financial reporting accuracy ensures financial visibility, allowing for better planning and attainment of strategic goals.

As noted earlier, Best-in-Class companies also capture higher early payment discount rates compared to their counterparts (please refer to the sidebar on page 4). This directly results in more savings for Best-in-Class companies than their peers. Best-in-Class companies report 8.9% annual percentage savings due to early payment discount capture, compared to 5.5% as reported by Laggards. This incremental savings directly contributes to the cash flow. As a matter of fact, Best-in-Class companies report 8.6% increase in operating cash flow over the past 12 months compared to 2.7% for the Laggards.

The correlation between superior AP performance indicators and the bottom line is no coincidence. Payable (includes AP and AR) is an important function within any organization and is the lifeline of cash flow. By enhancing existing payables processes, organizations can see the trickle-down effect to the bottom-line. It is truly a strategic function and for organizations and C-level executives hoping to enhance their financial forecasting accuracy and strategic goal attainment, payables is really the place to start. By relegating AP to a tier two, back-office function, executives and organizations might be missing a strategic piece.

A perfect analogy to conclude this section would be the game of chess. Even though some may not consider a soldier as important as the queen, players can only begin the game if they have the entire army and staff on board. Similarly, strategic initiatives cannot run on just one department or line-of business, all parts of the organization need to share the same strategic vision and need to be optimized to attain the end-goal.

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Related Research	
Integrated Accounting Platform: Achieving Accuracy and Efficiency at a Lower Cost; September 2013 *Beyond Payables: The Evolution of the Modern Financial Ecosystem*; September 2012	*AP Invoice Management in a Networked Economy*; May 2012

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