

Accounts Payable Best Practices

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Accounts Payable Best Practices

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IOMA's Report on Managing Accounts Payable

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For my candle in the wind,
my father,
Ron Schacht

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Introduction

Companies should be interested in implementing best practices in their accounts payable (AP) operations for the same reason that Willy Sutton focused on banks—it's where the money is. The fundamental structure of the AP function is that it is about a company's financial integrity. Those who disregard their AP operations will adversely affect their bottom line, either directly by

- Paying invoices more than once
- Paying charges that should have been borne by the supplier
- Failing to take advantage of special pricing arrangements
- Not taking earned discounts
- Being fined by states for failing to comply with escheat or sales and tax rules

or indirectly through

- Increased transactional costs
- Increased costs to resolve discrepancies
- Increased costs to fix errors
- Increased costs by failing to take advantage of new processes and technologies
- Failing to earn early payment discounts

OVERVIEW: FACTORS

The AP function has changed radically over the last 10 years, and it appears that the transformation will continue at least for the foreseeable future. The following are some of the factors affecting this transformation:

- Check fraud had reached levels that demanded not only a change in the way companies write checks but also the technology used to limit the scams.
- Companies looking for ways to keep costs under control have cut AP staffs to the bone.
- Technology has made a big dent in the amount of resources companies now need to allocate to transactional work.
- The concentration in a growing number of accounts payable operations is shifting from transactional processing to an analytical focus.
- The overall number of people working in AP is declining. That decrease is almost entirely in the clerical staff. Consequently, the professional level of these departments is rising.
- States, desperate for ways to increase their coffers without alienating the voters, have found companies failing to comply with unclaimed property and sales and use tax rules to be just the answer to their problems. They are aggressively pursuing them and, when they find them in noncompliance, auditing and fining them uncompromisingly. States now use third-party auditors in many cases. They also work together.
- The accounting scandals and the enactment of the Sarbanes-Oxley Act have raised the level of inspection at many companies, both private and public.
- The Internet

BEST PRACTICE PRINCIPLES

With reduced resources and increased scrutiny, implementing best practices in AP is more crucial than ever. Strictly focusing on cost is apt to get a company into trouble. While keeping costs down is a good idea, it is important not to let that be the only consideration. It is important that sufficient thought also be given to adequate controls, fraud prevention, and good vendor relationships.

To that end, in defining best practices, the following overriding principles will govern:

- Up-front controls
- A move toward minimizing paper
- Clear and easily traceable audit trails
- Minimal clerical data entry
- Transactional efficiency

This should translate into lower costs, in most instances.

BEST PRACTICES IN A THEORETICAL BEST PRACTICE COMPANY

If it were possible to select best practices simply on the basis of what's best and not taking into account corporate culture, existing procedures, financial limitations, and unique corporate procedures, here's what the list might look like:

- Implement e-invoicing for all invoicing.
- Use positive pay.
- Insist that all purchase orders be completely filled out before they are issued, and that Receiving completely check packing slips.
- Use workflow to route invoices for reviews with an escalating approval structure.

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- Have travel and entertainment (T&E) reports completed electronically; spot check rather than completely review each report; and make all employee reimbursements using direct deposit.
- Comply with all escheat and sales and use tax regulations.
- Make every payment possible electronically.
- Encourage all employees to be paid via direct deposit.
- Take advantage of all early payment discounts, but don't make any payments before the due date.
- Provide adequate resources for employee continuing education opportunities.

IMPLEMENTING BEST ACCOUNTS PAYABLE PRACTICE POLICIES

While the rest of this book examines AP functions in detail and spells out the best practices for each, this section will look at some overall best practice policies:

- Minimize or eliminate low-dollar invoices. This can be done through a variety of techniques, including:
 - Use of purchase cards (p-cards)
 - Making payments to certain vendors from statements rather than invoices
 - E-invoicing
- Institute strong up-front controls, eliminating the most back-end approval processes:
 - Completely filled-out purchase orders
 - Evaluated receipt settlement
 - Negative assurance
- Get rid of as much paper as possible using:
 - Imaging

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- E-invoicing
- A firm policy regarding where invoices should be sent first
- P-cards
- Consider outsourcing specialty functions, including:
 - Sales and use tax
 - Escheat
 - Duplicate payment audits
 - Value-added tax reclaim
 - Telecom and freight payment and audits
- Make as many payments as possible electronically, using:
 - Direct deposit
 - Automated clearinghouse credits and, where appropriate, debits
- Limit the number of phone calls coming into AP by:
 - Using online dispute resolution
 - Updating payment status on the Internet
 - Updating payment status using interactive voice response (IVR)
 - Publicizing payment timetables
 - Including an explanation slip with all short payments
- Don't forget the value employees bring to the AP function:
 - Motivate staff
 - Focus on morale
 - Allocate some resources for staff education

A WORD ABOUT BEST PRACTICES

It's fine to talk about best practices in a theoretical sense, but professionals who toil in the field know that sometimes what works in theory will not work in their organization. Some-

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times industry peculiarities stand in the way, and other times it might be the corporate culture or practices in another department. If the receiving dock does not do a good job at checking packing slips, it is pointless to implement a process that relies on accurate information from Receiving.

Thus, in this book, you will see discussions of best practices as well as what we refer to as “almost best practices.” These take into account that not all practices will work at all companies and offer an alternative to those who cannot implement the absolutely best practices.

We also include a discussion of those practices that definitely should not be used but, as many reading this know from painful experience, are in use in parts of Corporate America. Hopefully, by seeing these practices identified in print, some will decide to replace them in their own organizations.

WHAT’S INSIDE

The book starts at the beginning, reviewing the way invoices are processed. It identifies a number of potential problem areas and then offers best practice solutions. Some of the items may seem mundane to those not intimately familiar with AP. However, if they are ignored, expect duplicate payments and perhaps even fraud to increase.

At least for the present, as most AP departments have not made the leap to 100 percent electronic payments, checks dominate the payment landscape. If all aspects of this function are not handled properly, check fraud, duplicate payments, and processing costs will all increase. Also, the company may put itself in the position of being completely liable for any check fraud that does occur.

The mundane operational aspects of AP are reviewed in a way that focuses attention on issues that are sometimes ignored. A complete chapter follows this on one of the most im-

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portant, yet overlooked aspects of the purchase-to-pay cycle—the master vendor file. You would be surprised how often the master vendor file is not even an issue on the table—with disastrous consequences. With the renewed interest in internal audit and controls, thanks to the Sarbanes-Oxley Act, companies disregard their master vendor file at their own peril.

P-cards are one of the easiest innovations to understand, and companies everywhere are adopting them. The potential for growth in this area is staggering. Thus, it is imperative that those who use them do so correctly. The cost and time savings will be maximized if best practices are implemented from the beginning.

T&E is an area that has changed dramatically in the last decade. Online filing, the increased use of T&E cards, and other electronic initiatives have changed the way most of corporate America handles their T&E function. The chapter on T&E reveals some of the techniques used at innovative companies.

While few people think of AP and regulatory issues in the same breath, there are a few issues that, if not handled correctly, can bring trouble to a company. Specifically, in this chapter we take a look at 1099 reporting, sales and use tax handling and reporting, and unclaimed property, also called escheat. It is the last two areas, sometimes ignored by companies, that are drawing increased attention from the states.

As the AP function becomes more analytical, it is inevitable that companies begin to expect that the professionals who run AP take a cash management approach to the function. In some ways, paying too early is just as bad as paying too late. This chapter takes a look at some of the cash management initiatives that are increasingly falling on the shoulders of the AP department.

Although in many cases, AP was one of the last groups within some companies to get computers, they are making up for it in a big way today. Technology is making inroads into

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the department in an extraordinary manner. This chapter shares some of those innovations. We expect this area to continue to expand, especially as AP takes the lead in pushing for electronic invoicing and a move to electronic payments—away from the check standard.

Finally, successful AP departments are starting to realize that they have customers—both internal and external. By finding ways to deal with both, they are also improving vendor relationships. Those that do not make this leap can hurt the vendor relationship and increase costs as poor communications with other departments run up the dispute resolution bill.

Upon looking back at the items covered, it is truly amazing how much AP has changed in the last 5 to 10 years. This book attempts to identify the best practices that will make your AP department first rate.