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WHITE PAPER

AP Audits: A Key Component of a Successful Outsourcing Strategy

Businesses today constantly contend with change, whether growth, restructuring or other factors. Keeping pace with technology, whether it's GenAI, automation, or the countless digital tools available, requires a delicate balancing act. Businesses must adapt to market conditions, respond to competitive pressures, and navigate globalization, all while meeting client demands for faster, more personalized services. Add in regulatory changes, work force shifts, talent shortages and other economic factors into the mix, makes companies quickly realize time is the most precious of commodities.

As a result, many companies have turned to outsourcing key functions as a catch all for time and cost savings. While the concept is not new, its roots can be traced to the latter half of the 20th century, the practice had a tremendous upswing in popularity during the 2000s, due to advancements in technology and communication. Outsourcing is essentially entrusting a third party with the management of your business tasks, with IT, customer service, and accounting ranking as the top outsourced industries. The pandemic shifted the focus of outsourcing to strategic partnerships and value creation rather than just cost reduction. This period accelerated trends toward remote work and further highlighted the importance of flexible outsourcing strategies.

The Drive Towards Outsourcing

Accounts payable departments, while always busy, often feel increased strain during periods of rapid growth, staffing shortages and seasonal fluctuations. In recent years, this strain has been intensified by staffing shortages and regular influx/outflux of skilled personnel. To counter these issues, companies are increasingly outsourcing accounting tasks. Research estimates the global outsourcing market to rise to a projected $5.6 trillion by 2027, with the United States generating 36% of that total. Surprisingly, finance and accounting services represent 42% of US outsourcing, just slightly behind IT/customer support services (2024). Business Process Outsourcing - Worldwide. https://www.statista.com /outlook/tmo/it-services/business-process-outsourcing/ worldwide). Top US, destinations for outsourcing include the Philippines, India, Malaysia, and Poland, with Mexico and Brazil gaining traction as the concept of nearshoring continues to rise (experiencing a 28% increase since 2020).

Advocates for outsourcing are quick to cite cost savings as the primary benefit. “Some organizations use a commonly accepted estimate that the cost of processing a single invoice is equivalent to 30 minutes of employee labor. This provides a range of US$12 to US$35 per invoice, depending on your location and labor costs. (Jex, S. (2023). How much does it really cost to process an invoice? Quadient Blog. https://www.quadient.com/en/blog/how-much-does-it-really-cost-process-invoice). In this scenario, outsourcing alleviates both the cost and the time factor. Relying on their specialized outsourcing partner, now allows the remaining in-house AP staff to focus on AP exceptions, escalations, core business activities and alleviates the need to recruit, retain, and train skilled staff.

Detractors of the practice note that outsourcing is synonymous with a lack of controls. Financial and other key information and system access is now primarily in the hands of the third party. They are quick to point to data and cybersecurity as a huge concern. As the pandemic proved, this dependency, and therefore access to output can easily be disrupted due to geopolitical events, as well as time zone, communication barriers, and internet connectivity issues. Some third-party outsourcing employees are compensated based on the number of invoices processed in a workday,

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with no account for accuracy. With the growing trend of global outsourcing, third-party providers are now experiencing notable staff turnover.

Audits Essential to Success

The decision to outsource is a delicate one and should be carefully addressed on a company-to-company basis. What cannot be overlooked however, is the importance of conducting regular and comprehensive accounts payable audits regardless of the processing location or industry. Auditing outsourced payables is an essential practice for maintaining financial accuracy, compliance, and efficiency, while also mitigating risks and controlling costs effectively.

Key benefits of engaging in an AP audit include:

- Accuracy: Audits ensure invoices were processed and paid accurately, including all adjustments for applicable discounts, open credits, and rebates.
- Cash flow benefits: AP Audits not only identify overpayments and other missed financial benefits, but also recover those funds on a client's behalf.
- Compliance: AP Audits ensure transactions comply with legal and regulatory requirements, as well as internal policies and contractual agreements.
- Fraud: AP audits uncover irregularities in the payables process. Outsourced payables are vulnerable to fraudulent invoice processing, unauthorized transactions, potential internal collusion and lack of oversight.
- Process Validation: AP Audits review and comment on the integrity of the outsourced process and ensure agreed-upon standards are being met, identifying inefficiencies and offering recommendations and training for improvement.
- Transparency: AP audits ensure transparency and ensure the outsourced partner is accountable for their operations.

According to a study conducted by Broniec Associates based on recovery audits performed for clients with an outsourced AP function, they noticed the results tend to be higher due to processing issues. "The outsourced talent pool can be less experienced, and not as well trained or dedicated as that of the client company. Duplicate payments, missed credits, and discounts are often missed," said Adam Kimmerling, Quality Assurance Manager at Broniec Associates. The study found that outsourced payables can have a higher error rate, often ranging between 10% to 30% more errors compared to in-house managed payables. It noted that support and research are more difficult given the lack of direct access to data regarding outsourced accounts payable. In instances when an issue falls outside the outsourced team's core responsibilities, it often tends to be overlooked and left unresolved.

Conclusion

While outsourcing accounts payable can be a strategic move to enhance efficiency, reduce costs, and allow the in-house team to focus on core business functions, it has become essential to carefully evaluate potential partners and ensure they align with your needs and standards. A thorough due diligence process and clear service level agreements (SLAs) can help maximize the benefits and mitigate potential risks. Regular comprehensive audits of the AP function are a crucial and non-negotiable business best practice and integral when outsourcing. Neglecting regular AP audits can have significant negative consequences for a business now only limited to cash flow, but also damage to important vendor relationships and loss of reputation.

Bottom line for any organization, accurate and reliable financial information is crucial for making informed strategic decisions, and maintaining precise financial data is key to successful business operations.



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