

MEASURING YOUR AP PERFORMANCE: EFFICIENCY BENCHMARKS

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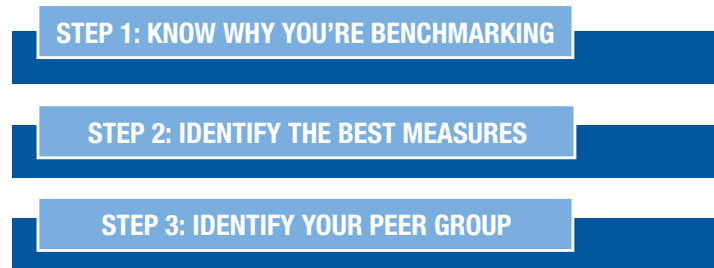
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INTRODUCTION

The first step in any improvement journey is to quantify where you're starting. That's a challenge for many AP leaders because it's difficult to recognize the most relevant measures and then determine who to compare your results against.

This report, which is part one of three, is designed to demystify the measurement and benchmarking process to help you get a jumpstart on your AP process improvement efforts. The findings are based on a two-year study conducted by IOFM of 388 AP functions.

FIGURE 1. KEY CONSIDERATIONS WHEN PREPARING TO BENCHMARK



STEP 1. KNOW WHY YOU'RE BENCHMARKING

Entire industries have been built on the premise: “If you can’t measure it, you can’t improve it.” That’s because to measure a process requires: identifying its beginning and end, defining the tasks that make up the process, and then considering the measures that will give you the most actionable insight to make and manage changes. If you can’t articulate those pieces, it means you don’t have visibility across the process and are going to have difficulty leading the process changes necessary to make improvements.

Measuring your performance is only half the battle. The next step is to compare your measurement results against AP and P2P functions most like yours. And identifying your peers – those with similar invoice volume, automation, and operational structure – is a crucial step in knowing if your performance is up to par.

It’s hard, but worth the effort. When done well, benchmarking addresses the two most critical questions you need to answer before making any changes to your AP process:

- 1. Is my team’s current performance good or bad (or somewhere in between)?**
- 2. And, if we were to make changes, how much improvement would be realistic?**

In this report we will answer those two questions in the context of four key efficiency benchmarks:

COST

- Paid on time rates
- Cost per invoice

STAFFING

- Invoices per FTE
- Staff per manager

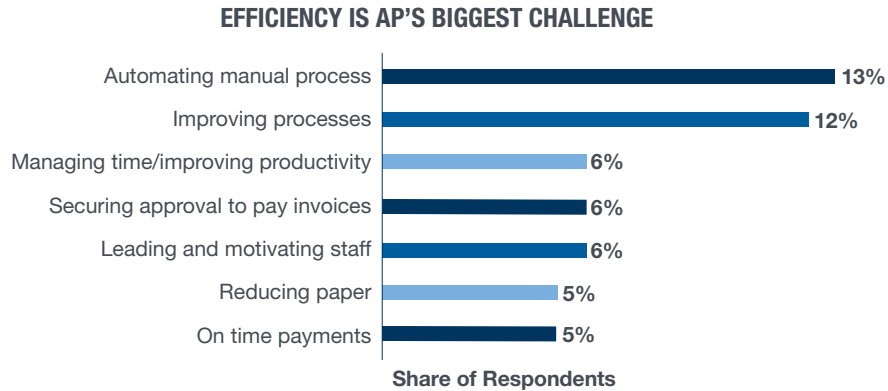
STEP 2: IDENTIFY THE BEST MEASURES

Actionable benchmarking is not an easy or simple undertaking. Few organizations have end-to-end systems that can pull all the required data, which means tedious manual work will be needed to extract, analyze, and report the data. There’s also political capital that will be spent to determine who will decide which measures to use, how the measures will be defined, who will have access to sensitive data, and what will be done with the results – especially if the results show the team is underperforming.

The effort required will vary by AP function, but there are a few common challenges experienced in payables departments across the marketplace. The most notable shared challenge is processing efficiency: finding ways to pay bills faster.

When given a list of dozens of AP challenges, six of the seven biggest challenges identified by AP leaders related to efficiency.

FIGURE 2. AP LEADERS’ TOP CONCERNS



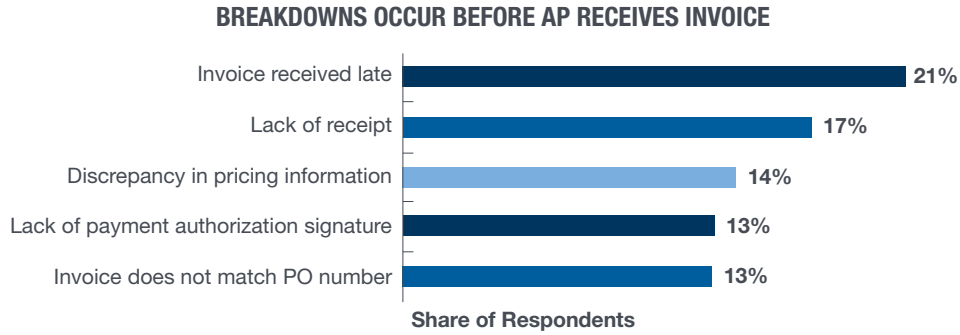
A deeper dive into the data finds that AP leaders are keen to improve the speed with which their teams process invoices because they are being pressured to do more with less. Among those AP functions IOFM studied for this report, the median number of invoices processed climbed 28% year-over-year while headcount dropped 12%.

With so much pressure on boosting efficiency, cycle time measures are crucial. But they are also among the most gamed statistic by AP leaders. IOFM found that 40% of the AP functions studied said they start the clock on their “paid on time” rates once AP receives the final invoice. While we understand the desire not to be penalized for the steps AP has no direct control over, such measures are cheating you out of actionable insights.

Here’s why. The bottlenecks that slow AP processing time the most are the things that happen *before*

AP receives the invoice: delays in AP receiving the invoice, whether the receipt exists and matches, etc. If you exclude these factors, your performance will look great, but it won't help you identify the core problems. Gaming the system only hurts your team because you aren't any closer to understanding what you need to address.

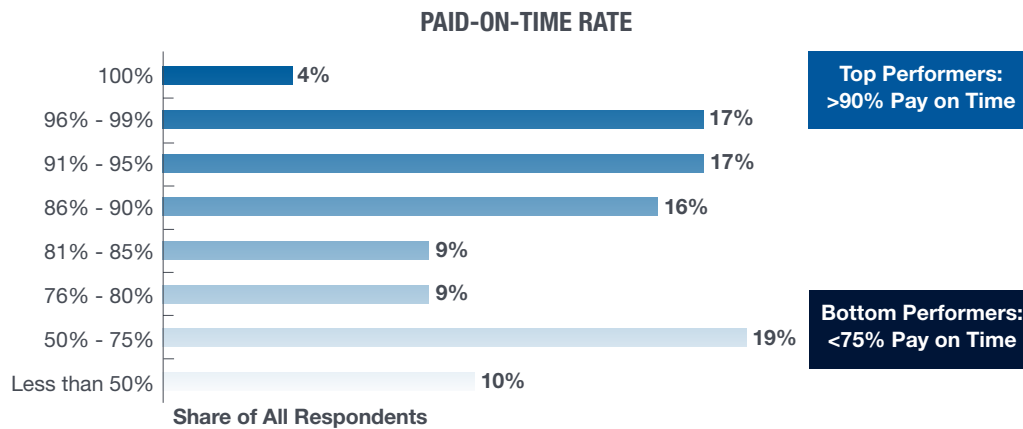
FIGURE 3. BIGGEST BOTTLENECKS TO AP PROCESS



Paying on time is an important measure because low performers risk upsetting vendors, or worse, paying late fees. Subpar performing teams are far less likely to capture early pay discounts (which usually require net 10 terms). And if you're challenged with paying bills on time (typically, net 30), you're far less likely to have time to fully address regulatory compliance, fraud and abuse, or cash management – the higher-value tasks AP can provide.

In analyzing only those AP functions that use “date of invoice” from which to begin the clock on cycle time (i.e., excluding those that game the statistic), IOFM defines top performers as those that pay more than 90% of their invoices on time, while bottom performers are those that struggle with as much as 75% of on-time payments; mid-tier performing AP functions fall between those two bookends.

FIGURE 4. FREQUENCY WITH WHICH ARE PAID ON TIME

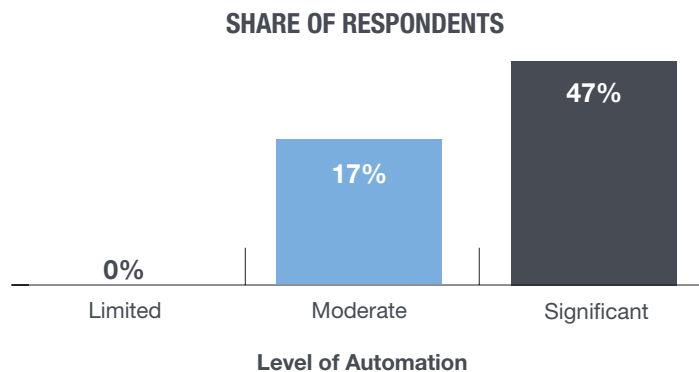


So, does this mean that you should set a goal of paying at least 90% of your invoices on time each

month and that if you're below the 75% mark, you're failing? Neither of those assumptions are correct for *all* AP functions. The answer – for this, and all metrics – is, it depends on your peer group.

That 90% benchmark would be a solid goal for those AP functions that have invested significantly in automation, but it would likely be unattainable for those with more manual processes. For those AP functions that have made only nominal investments in automation, none in our sample were able to pay 90% of their invoices on time. In other words, if your AP department processes paper invoices manually, it would be unrealistic to try to have a paid-on-time rate that high.

FIGURE 5. 'TOP PERFORMING' PAID ON TIME RATE, SPLIT BY LEVEL OF AUTOMATION



Setting accurate expectations and goals is crucial. This report is designed to identify achievable performance levels and highlight how much of an improvement would be realistic. Failing to do so harms your organization's ability to manage change. Moreover, holding an AP department to an unattainable expectation can kill morale and lead to involuntary staff turnover – especially of those that care the most.

In order to triangulate your peer group, IOFM provides three sets of numbers for every metric: invoice volume, level of automation, and operational structure.

There is no single numeric goal for all AP functions. If you're processing a few hundred invoices per year, there may never be a business case to be made for significant automation. And that's okay. There's no law that says you must achieve the level of a top performer.

If you know that high automation is not attainable, then you know that efficiency gains can be made by training your staff and tweaking your processes. However, if you have high invoice volume, you can more easily justify efficiency improvements by addressing your people, process, *and* automation.

STEP 3: IDENTIFY YOUR PEER GROUP

To enable apples-to-apples comparison, IOFM compares AP functions based on three peer groups:

- Invoice volume
- Level of automation
- Organizational structure

FIGURE 6. PEER GROUPS DEFINITIONS

HOW IOFM DEFINES AP/P2P PEER GROUPS					
	Low	Limited	Moderate	Significant	High
Annual Invoice Volume	<10,000	10,000-49,999	50,000-99,999	100,000-999,999	>1 million
Level of Automation¹ (Share of Invoices Received Electronically)	<10%	10%-29%	30%-50%	51%-80%	>80%
Organizational Structure	<u>Decentralized Operations:</u> distributed throughout businesses; AP does not operate as a single department		<u>Partially Centralized:</u> Some AP functions operated together, but many are still scattered across the business	<u>Centralized (but not SSC):</u> All AP functions work in a single group, but AP is not operating jointly with other related functions.	<u>Shared Service Center:</u> All AP functions are combined and working in tandem with all other operational functions.

FIGURE 7. PEER GROUP DISTRIBUTION

SHARE OF STUDY PARTICIPANTS WITHIN EACH PEER GROUP					
	Low	Limited	Moderate	Significant	High
Annual Invoice Volume	18%	22%	15%	38%	7%
Level of Automation (Share of Invoices Received Electronically)	21%	15%	14%	24%	26%
Organizational Structure²	<u>Decentralized Operations:</u> 7%		<u>Partially Centralized:</u> 16%	<u>Centralized (but not SSC):</u> 47%	<u>Shared Service Center:</u> 30%

1 For the purposes of this report, level of automation is determined based on the extent to which AP receives invoices electronically – i.e., enabled to be processed without any manual intervention. There are too many automation tools in the marketplace, variations of utilization (i.e., user training), and inter-dependence with other systems (i.e., outputs from procurement) to measure automation directly. E-invoicing as a proxy enables statistically viable comparisons because: 1) The more invoices received electronically, the more automation – of any kind – can be enabled; and, 2) E-invoicing tends to be one of the first processes addressed when investing in automation.

2 Because of the limited number of AP functions with no more than partially centralized operations, in some cases we opted to consolidate the four categories into two – “less centralized” (comprised of decentralized and partially centralized) and “more centralized” (comprised of centralized and shared service center AP functions).

The purpose of benchmarking – comparing your current performance against peers – is twofold:

1. To assess where you team is strong and where there’s room for improvement;
2. To gauge how much of an improvement would be realistic at the next stage in your journey.

With that in mind, IOFM suggests using all three peer groups to triangulate your current team’s performance, and then using the next higher level of AP automation as a basis to gauge what the next level of improvement could look like.

Understanding how much of an improvement in performance is realistic is crucial to establishing a ROI story to know if/when you’re ready to invest in the next level of automation.

Note: While higher invoice volume generally correlates with the decision to invest more significantly in automation, not all AP functions do so at the same pace. Below is the correlation between invoice volume and automation. (The percentages represent the share of respondents.)

FIGURE 8. CORRELATION BETWEEN INVOICE VOLUME AND AUTOMATION

		LEVEL OF AUTOMATION				
		Low	Limited	Moderate	Significant	High
Invoice Volume	High	10%	0%	0%	80%	10%
	Significant	14%	16%	14%	26%	31%
	Moderate	33%	17%	13%	25%	13%
	Limited	19%	11%	11%	36%	22%
	Low	26%	6%	16%	13%	39%

EFFICIENCY MEASURES: COSTS

PAID ON TIME RATES

IOFM takes two approaches to normalize cycle time measures:

1. We only include cycle time data for organizations that “start the clock” from date of invoice (excluding the 37% of the market that begin to measure when AP receives an invoice or the 3% that that measure after an invoice has been through a three-way match).
2. We track “percentage of invoices paid on time,” rather than the number of hours or days it takes to process an invoice to avoid significant data variability. Highly-automated AP departments can receive, sort, approve, and pay an invoice almost instantly; highly-manual AP departments require far more time. The approval time can also swing wildly based on POs vs. non-POs, utilization of P-cards, etc. Therefore, the key measure is how often AP departments’ processes enable them to meet vendors’ expectations.

FIGURE 9. SHARE OF POS PAID ON TIME, SPLIT BY INVOICE VOLUME

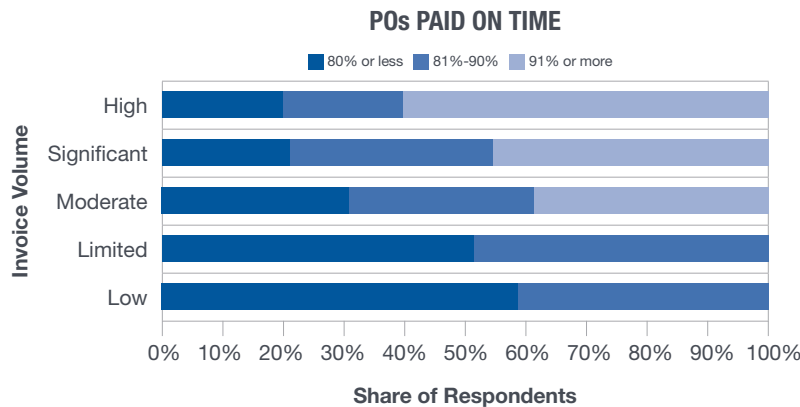


FIGURE 10. SHARE OF POS PAID ON TIME, SPLIT BY ORGANIZATIONAL STRUCTURE

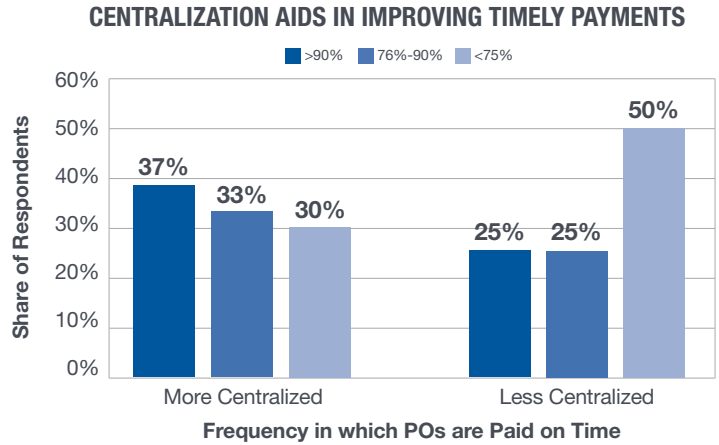
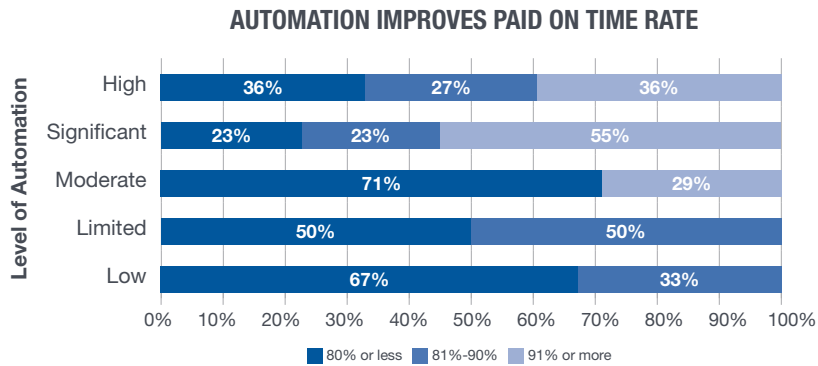


FIGURE 11. SHARE OF POS PAID ON TIME, SPLIT BY LEVEL OF AUTOMATION



COST PER INVOICE

IOFM takes two approaches to normalize cost per invoice:

1. To enable apples-to-apples comparisons across AP functions, we simply divided total base salaries of the AP team by the number of invoices that team processes per year. We defined the “AP team” by first asking a series of questions identifying who we’re counting, from mail room sorters, processors, vendor master file staff, through AP managers and directors, and then clarifying that we only wanted the base salaries of those team members.
2. We then conducted logical and statistical tests to validate the findings, removing any data that provided salaries that fell outside of our expected range.

We kept the definition simple to enable like-like comparisons. While the full cost per invoice includes employee benefits, one-time and on-going automation costs, other corporate overhead, etc., including those numbers would prevent us from making usable comparisons. That being said, we certainly would encourage you to calculate an “all-in” number, including procurement costs, to track internal progress on cost-cutting.

Below are the peer group data for this metric:

FIGURE 12. COST PER INVOICE, SPLIT BY LEVEL OF AUTOMATION

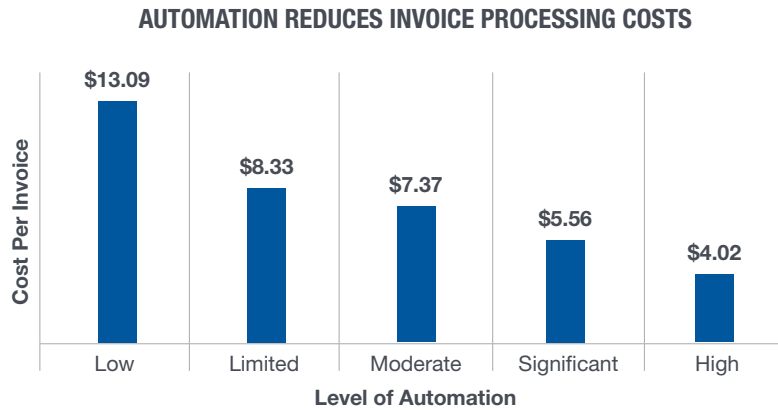


FIGURE 13. COST PER INVOICE, SPLIT BY INVOICE VOLUME

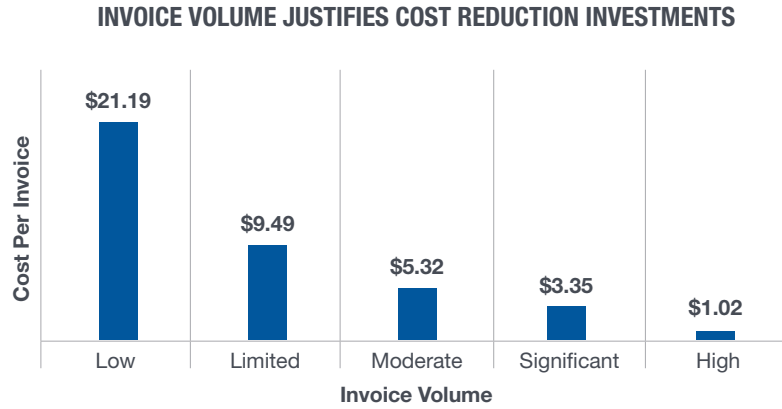
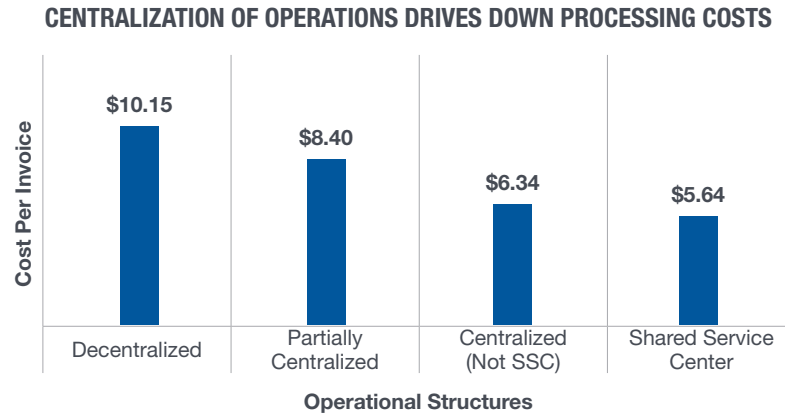


FIGURE 14. COST PER INVOICE, SPLIT BY CENTRALIZATION OF OPERATIONS



EFFICIENCY MEASURES: STAFFING

Costs are only part of the efficiency equation when benchmarking your AP team’s performance. It’s also important to know if you have the right number and mix of talent.

This section provides two metrics:

- **Invoices per FTE, to measure if you are adequately staffed**
- **Staff per manager, to measure if you are adequately balanced between junior- and senior-level talent**

INVOICES PER FTE

To normalize this metric, we eliminated organizations that outsource any part of their AP process to a third party.

The metric was then calculated using the remaining respondent data by simply dividing the annual invoice volume by the number of AP team members (using the same headcount methodology as described above when calculating invoice cost per FTEs).

FIGURE 15. INVOICES PER FTE, SPLIT BY LEVEL OF AUTOMATION

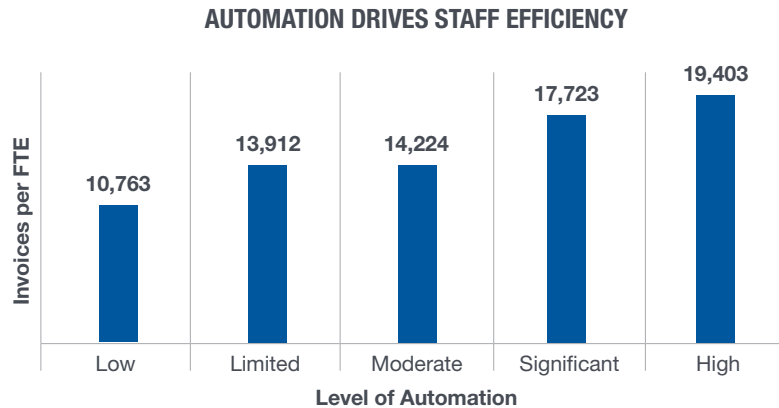


FIGURE 16. INVOICES PER FTE, SPLIT BY INVOICE VOLUME

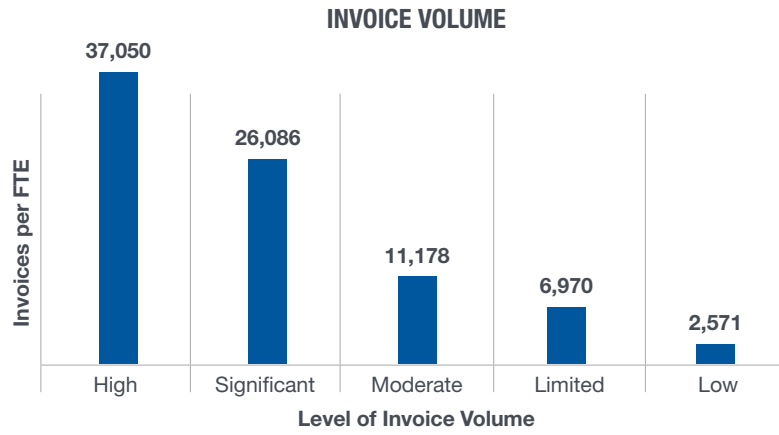
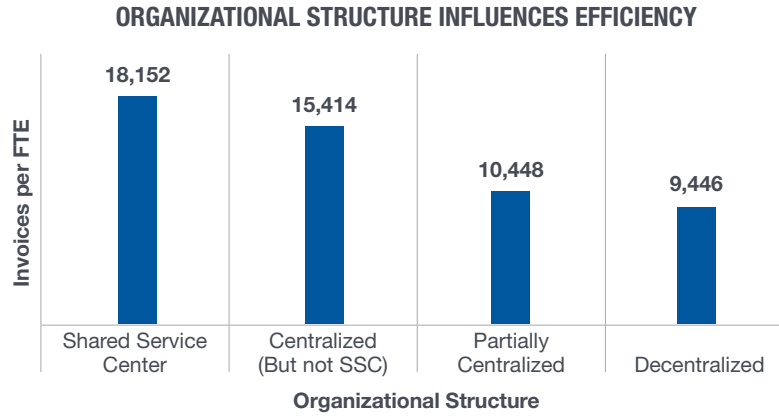


FIGURE 17. INVOICES PER FTE, SPLIT BY ORGANIZATIONAL STRUCTURE



STAFF PER MANAGER

The metric was calculated using same headcount methodology as described, and simply dividing the number of non-managers by the number of managers and higher. This measure is not intended to be used as a tool for firing or demoting anyone to reset your staffing mix. Instead, as you organically lose a team member through attrition, you should look to see whether you should replace that person with someone at the same level.

As you invest in automation, you'll likely need fewer lower-level specialists to do the work and more managers (as a percentage) to oversee the work.

FIGURE 18. RATIO OF SPECIALISTS TO MANAGERS, BASED ON LEVEL OF AUTOMATION

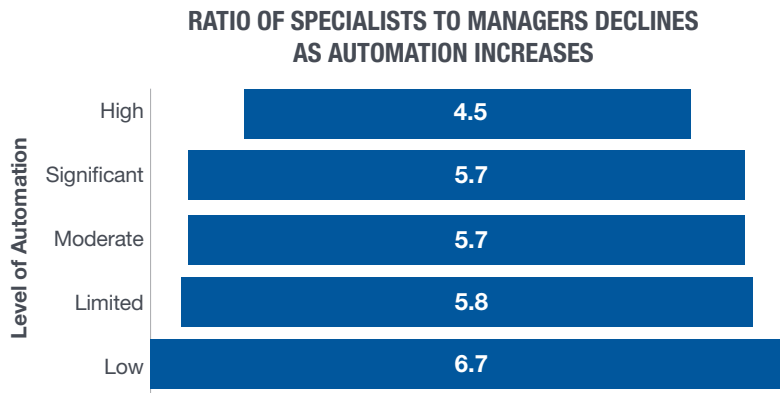


FIGURE 19. SHARE OF STAFF TO MANAGERS, SPLIT BY LEVEL OF AUTOMATION

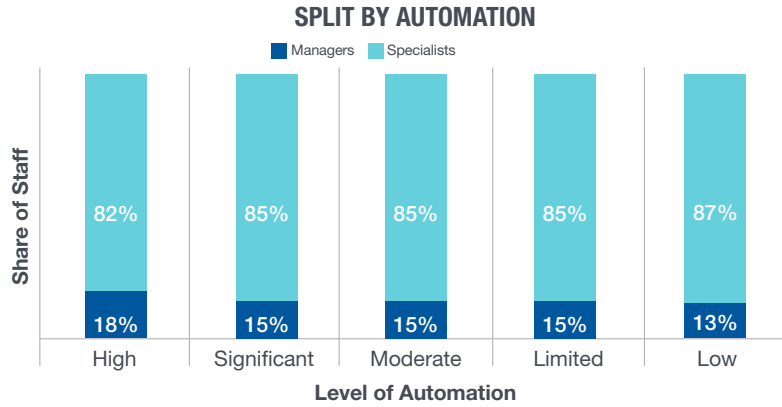


FIGURE 20. SHARE OF STAFF TO MANAGERS, SPLIT BY INVOICE VOLUME

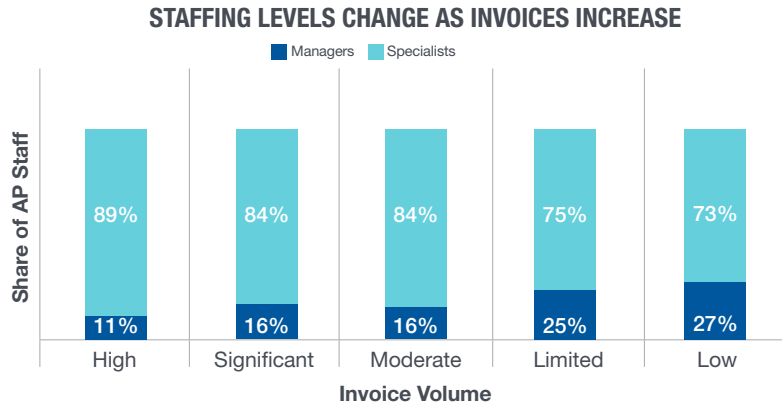
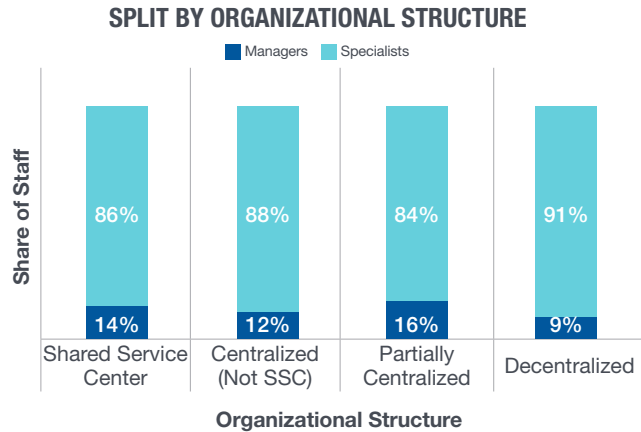


FIGURE 21. SHARE OF STAFF TO MANAGERS, SPLIT BY ORGANIZATIONAL STRUCTURE



EFFICIENCY MEASURES: SPLIT BY INDUSTRY

Of the 388 AP functions studied for this report, only five industry groupings were large enough to conduct valid statistical sampling:

- **Manufacturing**
- **Healthcare**
- **Finance**
- **Education**
- **Government**

The following section provides a high-level summary (bottom, mid-tier, and top-performing quartiles) for those five industries. IOFM suggests you still triangulate your peer group based on the categories in the earlier section (level of automation, invoice volume and organizational structure), but provides the following for additional context.

MANUFACTURING

FIGURE 22. COST PER INVOICE, SPLIT BY MANUFACTURING COMPANIES

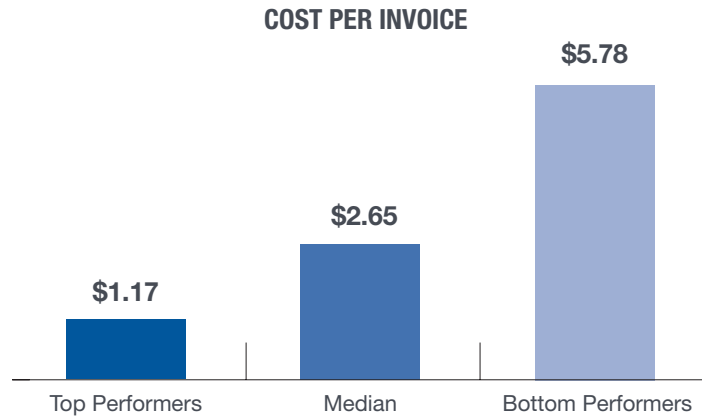
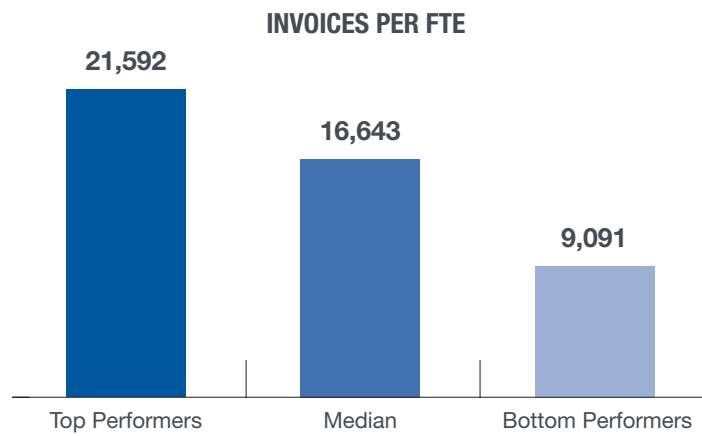


FIGURE 23. INVOICES PER FTE, SPLIT BY MANUFACTURING COMPANIES



HEALTHCARE

FIGURE 24. COST PER INVOICE, SPLIT BY HEALTHCARE COMPANIES

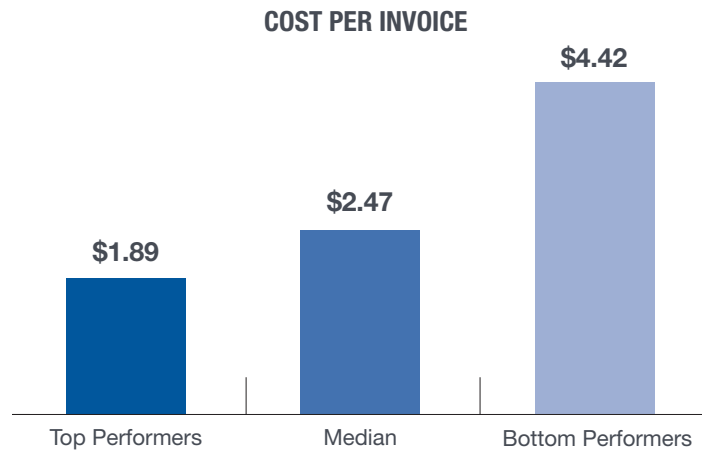
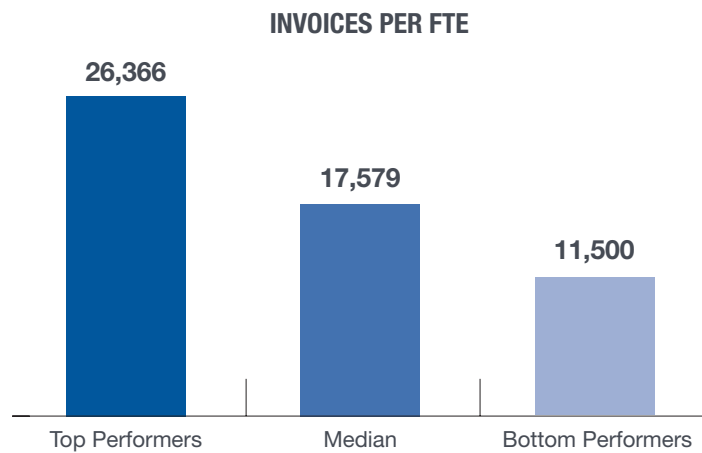


FIGURE 25. INVOICES PER FTE, SPLIT BY HEALTHCARE COMPANIES



FINANCIAL SERVICES

FIGURE 26. COST PER INVOICE, SPLIT BY FINANCIAL SERVICES COMPANIES

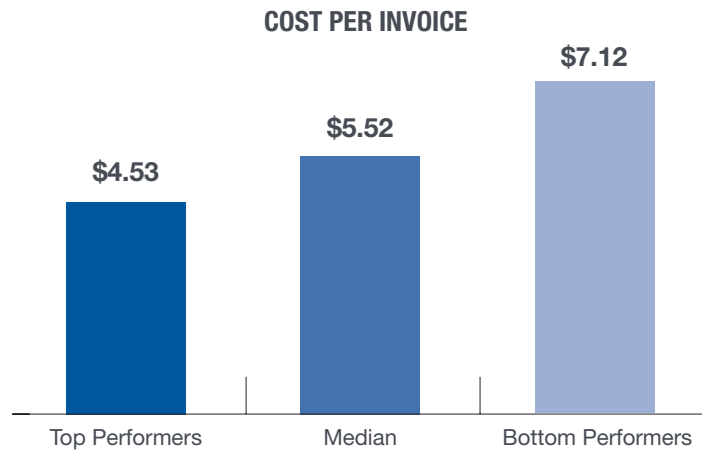
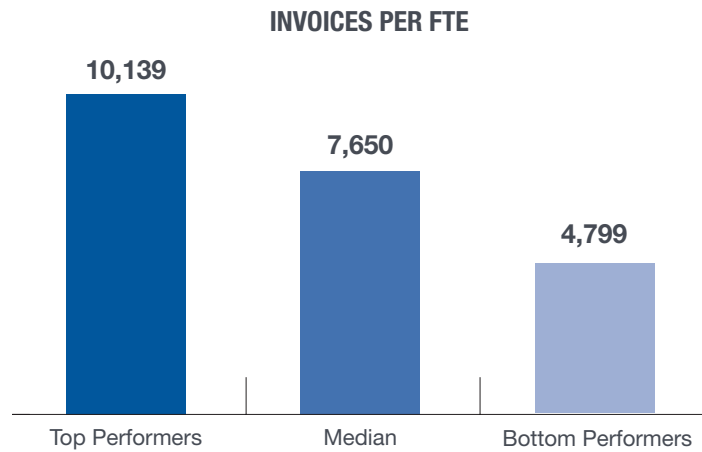


FIGURE 27. INVOICES PER FTE, SPLIT BY FINANCIAL SERVICES COMPANIES



EDUCATION

FIGURE 28. COST PER INVOICE, SPLIT BY EDUCATION ORGANIZATIONS

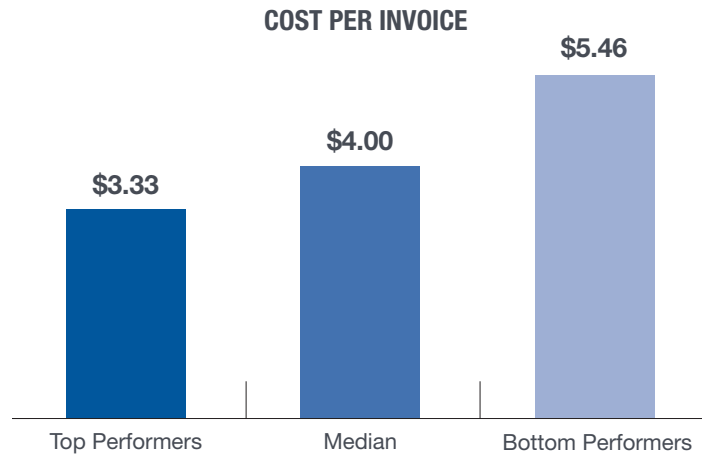
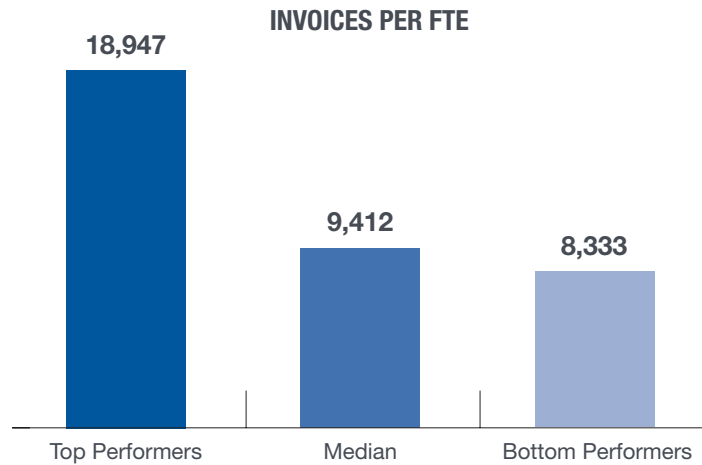


FIGURE 29. INVOICES PER FTE, SPLIT BY EDUCATION ORGANIZATIONS



GOVERNMENT

FIGURE 30. COST PER INVOICE, SPLIT BY GOVERNMENT ORGANIZATIONS

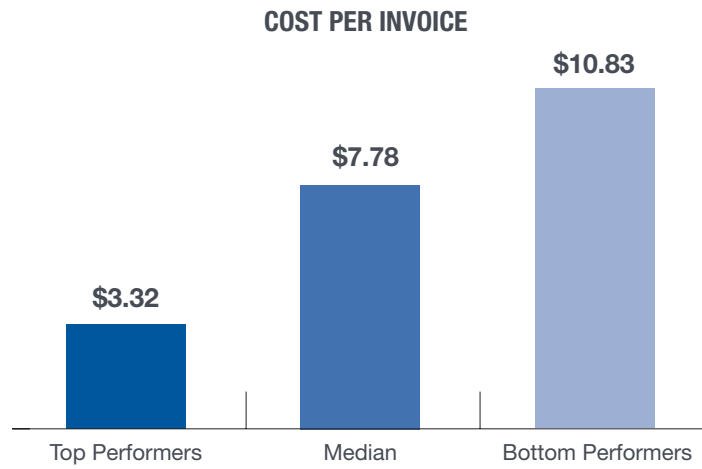


FIGURE 31. INVOICES PER FTE, SPLIT BY GOVERNMENT ORGANIZATIONS

