

Accounts Payable Risk Assessment: What Is It, How To Conduct One, and Best Practices To Mitigate Risk



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Anytime there's money, there's risk. And since the accounts payable department is responsible for paying vendors, suppliers, and others, the departmental risk level is elevated considerably.

Consider the following questions:

- Do you know what your accounts payable risk level is?
- Do you know how to assess the level of risk?
- What are the best ways to mitigate risk in accounts payable?

Understanding how to assess your accounts payable risk level and implementing ways to mitigate risk is an important part of accounts payable management.

What Are the Potential Risks of Accounts Payable?

The accounts payable department carries several risks that have to be properly mitigated to prevent unnecessary losses for your business.

The most common AP risks include:

■ What Are the Potential Risks of Accounts Payable



Fraud



Late or Missed Payments



Incorrect and Duplicate Payments



Rogue Spend

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• **Fraud**

Whether internal fraud or external fraud, the number one problem facing most accounts payable departments is fraud.

Accounts payable fraud takes many forms, including vendor kickbacks, fake vendors, false or inflated invoices, internal check fraud, or employees submitting exaggerated or false expenses for reimbursement.

In particular, a lack of oversight or not using segregation of duties in your accounts payable department can easily lead to fraudulent behavior on the part of the AP team.

Checks and balances need to be in place to prevent fraud.

For instance, an AP clerk who enters an invoice for payment should never approve the invoice or initiate payment.

▪ **Late or Missed Payments**

Late or missed payments may seem like a minor inconvenience, but for your vendors, one too many late payments can quickly become an issue, with your business suffering the consequences.

Chronic late or missing payments often leads to vendors changing your payment terms or even revoking credit privileges.

Late payments can also negatively impact your business's credit rating and make it more difficult to obtain good credit terms with other vendors.

▪ **Incorrect and Duplicate Payments**

Payments made in the wrong amount or duplicate payments can also cause problems.

Vendors may find it annoying to have to return a payment to their customers, while customers can often wait weeks or even months to have a duplicate payment issue resolved.

Data entry errors can also lead to payments made in the wrong amount, leading to cumbersome corrections or credit memos that need to be applied.

▪ **Rogue Spend**

Another area that can negatively impact your business is rogue spend.

Without the proper invoice approval channel in place, rogue spend, also

called maverick spend can be a common occurrence and can wreak havoc on your cash flow balance and the accuracy of your reports.

Any time a purchase is made without following proper AP processes is considered rogue spending.

This can be purchasing an item from an unauthorized vendor or purchasing an item or service for which the proper approval process has not been used.

Implementing invoice tracking, and a streamlined workflow system eliminates rogue spending in your business.

Why Is Accounts Payable a High-Risk Account?

Because accounts payable deals exclusively with company funds leaving the business, it's considered a riskier account than its accounts receivable counterpart which deals with money paid by its customers.

Any mistake in accounts payable is likely to result in a loss of money.

While risk can be mitigated, because of the nature of accounts payable, there will always be a certain level of risk attached to it.

One of the best ways to manage risk for accounts payable is to conduct a risk assessment, which can help pinpoint areas that need improvement.

We'll explain exactly what an accounts payable risk assessment is and how you can complete one for your business.

What Is an Accounts Payable Risk Assessment, and How Do You Complete It?

Similar to an accounts payable audit, a risk assessment examines current AP

processes including payment controls to pinpoint areas that need improvement.

Unlike an audit, a risk assessment also determines how best to optimize current processes, strengthen weaknesses, and create a more efficient operation.

To begin, an accounts payable risk assessment looks at two areas:

■ An Accounts Payable Risk Assessment Looks at Two Areas



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1. **Data verification** - which examines financial records to determine accuracy.
2. **Risk assessment** - which looks at current AP controls in place, notes missing controls, and other inefficiencies, and finally, determines what measures to put into place to effectively reduce or eliminate these risks.

To begin your AP risk assessment, you'll want to review the following:

To Begin Your AP Risk Assessment, Review the Following:



The Invoice
Receipt Process



How Invoices are
Recorded



Accounts Payable
Access



How Invoices are
Paid



Reporting

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• **The Invoice Receipt Process**

Invoices can be received in a variety of ways. Do most of your vendors and suppliers email you their invoices, or are they still sending paper invoices in the mail?

The most efficient way to receive an invoice is to have your vendors upload it directly into an AP platform that will automatically read the invoice and post the expense accordingly.

On the other hand, paper invoices can pose numerous risks including being lost or misplaced once received.

Invoice approval delays are also more likely to occur if you're still processing paper invoices.

If your business still uses paper invoices, consider this an area that needs to be improved.

• **How Invoices Are Recorded**

Does your AP staff use manual processes to record invoice data or do you

use an automated system that uses a combination of optical character recognition (OCR), AI, and machine learning to automatically record the invoice into your accounts payable system, without any data entry necessary?

While you'll still have to review scanned invoices for accuracy, particularly at the beginning, the number of errors will never come close to those made using manual data entry.

▪ **Accounts Payable Access**

Do you have the proper spending controls in place, or do staff members still order products and services without the proper approvals?

One of the best ways to prevent rogue spending is to restrict payables access to the appropriate staff members.

This means that when you create roles for employees, they are provided with access to only the tasks necessary to perform their jobs.

For instance, if one employee is responsible for paying invoices, they should not be able to approve invoices.

▪ **How Invoices Are Paid**

Once an invoice is approved, who enters the invoice into the system for payment? Who approves the invoice for payment?

What staff member processes the checks, signs the checks, or initiates the ACH transfer?

If you have one staff member doing all of that, you're at high risk for internal fraud or inaccurate payment processing.

▪ **Reporting**

It's important that accounts payable reporting is accurate, but if a stack of invoices is sitting in someone's in-basket waiting to be approved, they aren't going to be included in your reporting totals.

AP automation allows you to account for an invoice as soon as it's received, ensuring reporting accuracy in real-time that shows committed spend totals.

Real-time reporting also prevents you from processing duplicate invoices because the prior invoice is still not yet in the system.

How Do You Mitigate Risk in Accounts Payable?

The best way to mitigate risk in accounts payable is to have processes in place that can help mitigate risk.

These processes, called internal controls, are a set of measures used to help a business manage its finances while significantly reducing risk.

Accounts payable internal controls include:

■ How To Mitigate Risk in Accounts Payable



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1. **Obligation To Pay Controls**

Obligation to pay controls are used to verify the accuracy and authenticity of every invoice that's received.

This is the very first step in the AP process and perhaps the most important.

2. **Data Entry Controls**

Data entry controls use a set of established guidelines to ensure accuracy and eliminate common issues like duplicate payments.

For example, if you receive an invoice with the number 0001234, without guidelines on how to record the invoice, one clerk may skip the leading zeros while the other will include them, meaning that a follow-up invoice may be recorded and paid twice.

Other data entry controls can include always capitalizing any letters in the invoice or stating that the invoice number has to be entered exactly how it appears on the invoice.

3. **Payment Controls**

Once an invoice has been approved, it still needs to be paid. Who approves payment in your AP department?

Is it the same person who approved the invoice or the same person who entered it? It shouldn't be.

Having proper payment controls in place means that the person authorizing payment is not the same person who approved the invoice, nor is it the same person who entered the invoice in your accounting software application.

What Are the Best Practices for Establishing Internal Controls?

Before you can implement internal controls, you'll need to identify weak spots in invoice processes starting at the very beginning.

What Are the Best Practices for Establishing Internal Controls



Invoice Receipt and Initial Processing



Separation of Duties



Three-Way Matching



A Streamlined Invoice Approval Process

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• Invoice Receipt and Initial Processing

One of the areas that requires close examination is the invoice receipt process. How much time does it take for AP to receive an invoice from a vendor?

Do paper invoices have to be routed to multiple departments before they're received by AP, or do they come directly to the AP department for processing?

Are invoices entered into the system before or after they've been approved (it should be after) Looking at these processes can help you create internal controls.

• Separation of Duties

Perhaps the most important control in accounts payable, separation of duties ensures that essential AP tasks are performed by multiple employees.

Each AP staff member should have dedicated tasks that they are responsible for, with each working together to create a system of checks and balances.

• **Three-way Matching**

Three-way matching helps to verify the accuracy of an invoice, comparing details against those of a corresponding purchase order and shipping receipt.

When the documents do not match, the invoice will need to be investigated.

• **A Streamlined Invoice Approval Process**

One of the biggest complaints when it comes to processing accounts payable is the amount of time it takes to process the invoice from initial receipt to payment. One area that causes the most delays is the invoice approval process.

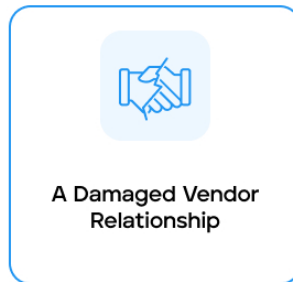
When using paper invoices and a manual AP system, invoices can get lost in transit, sit on someone's desk for days or even weeks before being approved, or be routed to the wrong individuals after approval.

The best way to ensure a streamlined, accurate invoice approval process is to use an automated AP system that automatically sends invoices to the correct approvers.

What Are the Consequences of Not Assessing and Mitigating Risks in Accounts Payable?

Not adequately addressing risk in accounts payable can create numerous issues for the department and your business including:

What Are the Consequences of Not Assessing and Mitigating Risks in Accounts Payable



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• **An Increase in Fraudulent Payments**

If outside suppliers or employees know that there are no safeguards in place, the possibility of fraud increases.

• **A Damaged Vendor Relationship**

Everyone wants to be paid accurately and on time for the goods and services they provide.

Human error alone can cause lost or misplaced invoices, late invoice payments, or payments made in the wrong amount, all contributing to a damaged relationship with a vendor or supplier.

• **Inaccurate Financial Reporting**

Internal budgeting and forecasting rely on financial statements being accurate. But so do outside sources such as vendors that are determining your creditworthiness along with banks and other lenders.

Investors also determine whether they wish to invest in your business by examining your financial statements.

If they're not an accurate reflection of your business, it can cost you great

terms from a vendor or a bank loan or line of credit to grow your business.

What Are the Best Practices for Accounts Payable Risk Assessment?

Examining every relevant level of your accounts payable processes is essential for completing an accounts payable risk assessment.

Unfortunately, instituting best practices when using a manual AP process system is cumbersome and likely to reduce risk less than you would like.

Instead, consider implementing accounts payable automation software like PLANERGY, an automated procurement application that uses OCR, AI, and machine learning to record and process invoices in real time while eliminating lost or misplaced invoices and data entry errors.

Investing in your business by automating AP also creates a more efficient AP department, while providing data transparency, and a complete audit trail.

Automating your AP system, eliminates the traditional roadblocks businesses face when manually processing AP, while reducing errors, and ultimately, risk.

What's your goal today?

1. Use PLANERGY to manage purchasing and accounts payable

We've helped save billions of dollars for our clients through better spend management, process automation in purchasing and finance, and reducing financial risks. To discover how we can help grow your business:

- Read our case studies, client success stories, and testimonials.
- Visit our Accounts Payable Automation Software page to see how PLANERGY can automate your AP process reducing you the hours of manual processing, stopping erroneous payments, and driving value across

your organization.

- Learn about us, and our long history of helping companies just like yours.

Book a Live Demo

2. Download our guide “Preparing Your AP Department For The Future”

Download a free copy of our guide to future proofing your accounts payable department. You’ll also be subscribed to our email newsletter and notified about new articles or if have something interesting to share.

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3. Learn best practices for purchasing, finance, and more

Browse hundreds of articles, containing an amazing number of useful tools, techniques, and best practices. Many readers tell us they would have paid consultants for the advice in these articles.

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