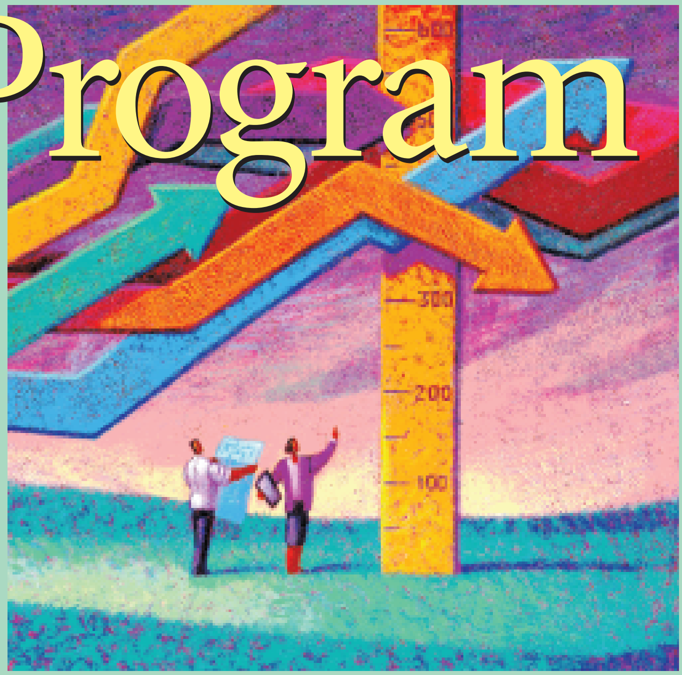
# Creating a Best-in-Class KPI Program




It can help you run operations efficiently and maybe even save money.

BY JANI KASKINEN

As all management accountants know, to run operations efficiently it's essential for organizations to get their financial houses in order. They must have real-time visibility and control as well as effective management of their cash flow, financial commitments, and payments to know where the company stands at any given moment. And under the Sarbanes-Oxley Act (SOX), companies not only must meet set levels of compliance in these areas, but they also must demonstrate their continual improvement of financial processes.

ILLUSTRATION: ROB COLVIN/ARTVILLE

Outstanding organizations, however, are already committed to the continuous improvement of their financial operations. They strive for excellence and understand that knowledge and control of their financial status lead to sound financial health as well as the ability to make better business decisions.

One way to achieve continuous financial improvement is to establish a program of key performance indicators (KPIs). Since it's difficult to improve what you can't measure, a KPI program enables a company to measure current performance against goals and benchmarks to understand the organization's strengths and where it's falling short. Best-in-class organizations use KPIs to improve poor performance as well as enhance positive results on an ongoing basis to achieve continuous improvement.

Purchase-to-pay, which includes purchasing, accounts payable, and travel and expense management, is an important area that can benefit from a KPI program because it provides key insight into cash flow and spend management. A KPI program in purchase-to-pay enables companies to implement continuous improvement and cut operating costs.

According to The Hackett Group, a strategic advisory and benchmarking firm, finance departments that measure their performance intensively are showing significantly better results in decreasing costs and improving productivity. They also benefit from improved quality and enhanced customer service.

## SOME BEST PRACTICES

If you want to establish an effective KPI program in purchase-to-pay, you can use this roadmap, which includes the following best practices:

- Set program goals;
- Select balanced, actionable KPIs;
- Align your KPIs with your strategy;
- Establish benchmarks;
- Determine your baseline;
- Determine what you need to view;
- Establish reporting needs.

### Set Program Goals

Before you begin, consider what you want to accomplish, and set your priorities. Although you can measure and assess more than 115 metrics, it isn't practical to try to focus on all of them at once. Consider your financial goals. Where will you get the most strategic benefit? Understand that a successful KPI program requires buy-in from affected departments and that the information won't be valuable unless it gets used, so get input from key individuals early in the process.

Reach out to the people who are responsible for gathering the KPIs, those who will use the information, and the employees who will be impacted. Conduct interviews with these stakeholders, such as executives, heads of operations, and team leaders. Find out which areas within your purchase-to-pay processes are effective, which are lacking, and the stakeholders' wish lists of improvements and priorities. In addition, determine how they could use the KPI information within their departments to help improve their processes. The selection of KPIs and means of communication can be tailored to specific job functions and levels to provide meaningful information based on user needs.

### Select Balanced, Actionable KPIs

No single KPI can provide a comprehensive view of the overall situation. That's why a performance management system should focus on multiple factors including cost, productivity, quality, employees, supplier-specific issues, and strategic alignment. When determining strategic alignment, for example, you might consider such issues as the number of suppliers that compose the bulk of total spend or total transactions; the number of suppliers that have less than a specified number of transactions; the use of controls such as purchase orders (POs), goods receipts, or invoices; the use of standard end-to-end processes; etc.

It's important to measure the various factors that can influence a particular KPI. For example, a company may want to improve its invoice processing function. To determine how it's performing in this area, the company should measure the cycle time in approving invoices, the percentage of invoices that have purchase orders or contracts associated with them, etc. This will enable the company to know whether there's a problem in this area and to determine the cause.

When establishing KPIs, assess the use of controls, including contracts, purchase orders, goods receipts, and invoices. Also consider trend analysis, target setting, and tracking—all key management practices that ensure the continuous improvement of overall end-to-end process performance.

In its annual Finance Shared Service Survey, The Hackett Group polled participants on which KPIs they use in the accounts payable process. The most common ones encompass measures focused on productivity cycle time, cost, error rates, and agreed service levels. These common

## Figure 1: Reporting Dimensions for a KPI Model for Purchase-to-Pay

**COSTS**
- Cost per FTE
- Total cost of operations
- Procurement cost control and optimization
- Costs per transaction
- Working capital effects

**QUALITY**
- Customer satisfaction and audit ratings
- Input quality
- Output quality
- Backlog
- Process automation
- Effectiveness

**STRATEGIC ALIGNMENT**
- Preferred supplier
- Controls
- End-to-end process strategy

**PRODUCTIVITY**
- Number of FTEs
- Transactions per FTE
- Cycle times
- Automation and presentment

**EMPLOYEE**
- FTEs and span of control
- Staffing mix
- Workforce development
- Employee satisfaction

**SUPPLIER SPECIFICS**
- Baseline information
- Processes
- Automation
- Supplier quality
- Internal quality
- Payment term optimization

measurements include incoming invoices per full-time employee (FTE), the time between invoice receipt and posting, the percentage of invoices posted within a set number of business days, the percentage of wrong payments, and the cost per invoice processed.

Make sure that you select KPIs you can act on because, after all, the purpose of the program is to improve the processes you have in place.

### Align Your KPIs with Your Strategy

Once you've conducted interviews, determine which KPIs will have the greatest impact on your organization. Which align most closely with your business goals? Once you've determined this, prioritize the KPIs you want to measure. Also make sure that you align the KPIs with the end-to-end process strategy, which includes supplier-base optimization, supplier and commodity classification, and a risk-balance strategy.

There may be a natural order in which you should approach your KPIs. For example, you first need to measure how many invoices a full-time employee processes before you can measure the cost associated with processing each invoice.

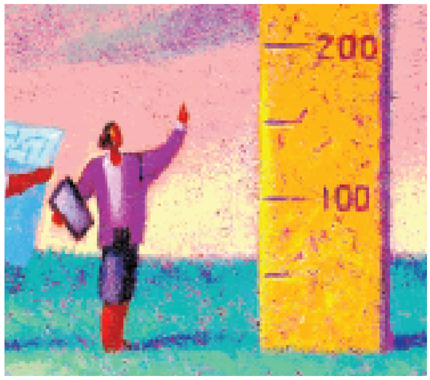
### Establish Benchmarks

Determine the benchmarks you'll use for each KPI. External benchmarks are typically determined based on industry standards. Internal benchmarks are usually based on internal goals, which take into consideration many factors, including the technology you have in place, your financial value chain, and processes.

### Determine Your Baseline

When you begin a KPI program, identify where your organization currently stands on each indicator. Measure each KPI against current processes, such as number of invoices you are processing, time per invoice, cost per invoice, etc., so you have a baseline for measuring future performance. By measuring performance at the outset, you can track change, easily reassess business cases, and evaluate performance levels more objectively. This will also allow you to mitigate risk by being able to see early-warning signs and conduct a root-cause analysis of any problems you uncover.

Once in place, the KPI program uses tailored scorecards against which you can monitor the success of current projects and easily see the analysis of the results.




### Determine What You Need to View

In establishing your dashboard, consider the information you need to display, including processes by time period, division, and employee. Determine which data you're measuring and where it's coming from—for example, the enterprise resource planning (ERP) system and human resources (HR) databases—and make sure you have an efficient way to pull the data from the different systems. An automated enterprise purchase-to-pay system will provide an ideal solution for this. The dashboard is an indication of your current status and whether you're meeting your benchmarking goals.

Ensure that the dashboard not only displays key information that provides all stakeholders immediate views into where your organization stands with respect to the KPIs but that it also allows them to create chains of KPIs to get to the root cause of a specific issue. For example, if a company wants to find out why scan-to-payment takes such a long time, it can create a chain of KPIs measuring scan-to-workflow, workflow-to-approval, and approval-to-pay. The ability to create chains of KPIs reduces risk by allowing your organization to see potential problems early on. It also enables you to conduct a root-cause analysis to plan possible solutions to the problems.

### Establish Reporting Needs

Different subsets of the KPI model are used for different recipient levels in your organization (see Figure 1). You can select specific KPIs tailored to the recipient's needs and as a means of communicating the KPIs. Executives are primarily interested in strategic information, such as costs, value-add to the organization, compliance, and measures indicating how well the company strategy is supported. Typical cost measures on executive scorecards are overall cost of the function, average annual labor costs, and cost per transaction. Executives will probably be interested in how improved purchase-to-pay processes will increase working capital and save on external spending. Information about credited days and debited days will enable them to manage cash flow more effectively. And information on compliance measures will indicate areas for improvement.

Heads of operations use the scorecard information to report to executives as well as to manage operations. In addition to the relevant measures reported on the executive scorecard, this group needs to see project-specific measures and productivity, process, and quality indicators regarding the workforce and employees. They also are interested in indicators of the overall quality of services (e.g., customer satisfaction, percentage of erroneous purchase orders, number of inquiries normalized by number of invoices) as well as indicators used for root-cause analysis such as reasons for long cycle times. Information on the workforce and employees provides the heads of operations with details such as staffing mix and span of control, average training hours per FTE, and indicators of employee satisfaction (e.g., satisfaction rating, overtime per FTE).

Define project-specific indicators based on the objectives set for the project. It's a best practice, however, to define at least one KPI per key project so it can be tracked, monitored, and reassessed as appropriate.

If you apply performance management down to the team-leader level, heads of operations need to track the KPIs that the team leaders are measured against. Heads of operations—or dedicated resources managing the service-level agreements (SLAs)—also need to track the performance indicators defined within the respective SLAs. In most cases, separate scorecards or reports should be defined for SLA-related reporting. In addition, team leaders should have scorecards focused purely on the relevant operational and project-related measures for which they're responsible and that address productivity and quality dimensions. Cost- and employee-related measures are typically less important for the individual team leaders.

## LEVERAGE TECHNOLOGY

Automated KPI tools enable organizations to effectively measure, assess, and report on their KPIs and work toward continuous improvement. Here are some considerations and best practices in establishing technology solutions to support a KPI program.

### Choose Software that Provides the Data You Need

Software is a very effective tool for driving efficiency in the purchase-to-pay process and can add value in several key areas of KPI reporting. Automated solutions typically provide standard definitions for KPIs within the purchase-to-pay process. This helps solve the problem of interpreting and comparing KPIs by giving you apples-to-apples comparisons.

Purchase-to-pay software provides a quick, automated way to extract the data that you want to measure and analyze. Some software solutions will deliver purchasing and invoice processing information in real-time so you can see what's happening with your purchase-to-pay processes at any given moment. Companies should choose technology that provides the data needed to build the KPI, such as recording actions and time-stamping each process. Additionally, automated tools enable you to conduct meaningful analysis of a particular measure, see the root-cause analysis, and implement changes.

Technology also is critical in helping organizations implement process changes. For example, if you want to specify the dollar amount of invoices that particular individuals can approve, you can set those parameters into your invoice processing system.

### Establish a Flexible Reporting Solution

Some software can offer flexibility in selecting KPIs and communication channels for the three key stakeholders I mentioned earlier—executives, heads of operations, and team leaders. The KPIs also can be tailored to a departmental and individual level.

Here's the type of flexibility that your software system should provide:

- Multiple scorecards should address the same KPI goals but display information differently based on the stakeholder.
- The system should give you the ability to easily make changes to scorecards, such as when employees' roles change and they need to see a different set of KPIs.
- External data from other sources must be easy to integrate into the system.
- Multiple ways of viewing the data and conducting analyses should be supported. For example, if you are interested in productivity of an FTE, you should be able to view it by day, month, year, etc.
- Flexibility of analysis type is important. This enables comparisons between different organizational units and against predefined targets and scorecard reports, as well as the ability to create chains of KPIs and conduct root-cause analysis.

## IDENTIFY NEXT STEPS

Once you've implemented a KPI program, determine how you want to further develop it. Consider the following:

In the spirit of continuous improvement, it's important to review your KPI program at least annually. Once you've achieved some of the benchmarks you've established, where do you go from there? Do you want to further improve the KPIs you've selected, or do you want to choose new or additional ones? Poor performance must be highlighted and followed up with a root-cause analysis to ensure that the same patterns aren't repeated. Positive results should be fed back to the appropriate individuals and departments, such as accounts payable, purchasing, and your expense management group. With this information, they can maintain the success of your processes and perhaps institute incentive programs to achieve even greater results. Best-in-class organizations never stop striving for excellence. Once they reach their goals, they often raise the bar on their achievement or look for new areas they can improve.

## LOOK FOR STRATEGIC RELATIONSHIPS

Once you've made progress with individual KPIs, you might want to consider linking related processes together. For example, you might look at the relationship between cost and quality and then determine a threshold that you want to maintain between the two.

KPIs are particularly useful in shared service center (SSC) environments in which services are centralized and provided throughout the entire organization. Purchase-to-pay shared service centers need to deliver on service-level agreements and must find a way to measure, manage, and continuously improve their processes.

## SIGNIFICANT RESULTS

A best-in-class purchase-to-pay organization uses a KPI program along with technology to streamline and automate processes as well as establish real-time visibility, cost control, and regulatory compliance. When combined with a focus on process improvement, a program of measurements can be a powerful tool that delivers significant results. By establishing a KPI program of measurement, you'll have greater insight into how you can improve your processes. According to The Hackett Group, operations that are measurement intensive are more likely to improve customer service, process quality, and productivity, as well as lower costs. The end result: Your organization can benefit from real-time visibility and control and be well on its way to greater operational efficiencies. ■

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