STOP LEAKING PROFITS:

Best Practices for Establishing Company Spending Policies

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INTRODUCTION

CALL IT THE YIN AND YANG OF A THRIVING SMALL OR MIDSIZED BUSINESS. COMPANY EXECUTIVES ARE FOCUSED ON TWO PRIMARY AREAS: GROWING REVENUES AND MANAGING EXPENSES.

Whether business is booming; growing at a manageable rate; or facing financial challenges, top executives know that without oversight and involvement, spending can easily spiral out of control.

Consider the spending habits of many small and midsized companies. Spending occurs in every aspect of a business. It is not uncommon for individuals, departments and offices to purchase the same items from multiple vendors at varying costs, wait until the last minute to obtain airline tickets and submit expense reports with questionable items.

The finance team continually reminds everyone about obtaining approvals for purchases and booking travel through the preferred provider. But no matter how hard finance pushes, it seems as if the sales force thinks the Four Seasons is the only hotel in New York and employees continue to buy office supplies on an ad-hoc basis without care about costs.

One of the best ways to stop the seemingly endless cycle of unapproved and over-the-limit expenses or to empower more people to spend on behalf of the company without fear of losing control is to establish company spending policies. Without them, it is difficult to set boundaries and create controls, much less enforce them.

WHY COMPANY SPENDING POLICIES MAKE SENSE

The benefits for establishing company spending policies are substantial. A spend management study from TripleTree, a research-based investment banking firm, shows that a one-percent decrease in operating costs has ten times the impact on profitability as a corresponding increase in revenue.

A study from Gartner, Inc., a research and advisory firm, cites a similar outcome. The report found that a five-percent reduction in operating costs in the expense-management process has the same effect as a 30-percent increase in sales.

Creating better cost controls is a high priority for many small and midsized businesses. According to an American Express Survey, 78 percent of the mid-sized companies it polled earlier this year said they planned some or many improvements to cost-management methods over the next year; while another 13 percent considered cost management their top target for improvement. In line with their overall design for tighter cost management, 74 percent surveyed said they'd improve monitoring employee compliance to spending policies.

But for many finance executives in small and mid-sized companies, the thought of imposing spending policies can produce a great deal of anxiety and dread, according to PayStream Advisors, an expense management research and advisory firm. Will employees buy into the policies? Can the company get away with requiring limits on what can be spent and with whom? Will the policies be too rigid? Will they be enforceable? What will happen if employees don't adhere to the policies?

As every business matures, however, there comes a time when the need for spending controls outweighs the apprehension and the anticipated resistance to change that imposing policies may produce. The good news is that much of the concern about building company spending procedures can be avoided with a few strategies to support the process.

CREATING SPENDING POLICIES

There are no hard and fast rules to crafting company spending policies. It should be viewed as a creative process where common sense prevails. The end product should be considered a dynamic document that can be refined by the management team as needed to better fit the organization. Companies have more success with employee compliance when spending policies reflect corporate culture.

Consider the breadth of the policies; what components of company spending will be included. Many business and finance executives initiate spending controls by establishing travel expense management processes. While travel and entertainment can account for up to ten percent of a company's total operating expenses and is often second only to payroll, controlling spending doesn't stop there.

A more holistic approach considers controls for all company expenditures, including travel and entertainment and purchasing. It should also take into account what, if any, policies may need to be applied to payroll and the piles of recurring invoices for leases, electricity, telecommunications, and more that flood the accounts payable department.

At the onset, focus on what the company is trying to accomplish, rather than the length of the document. Successful policies can be as short as one or two pages or can be quite extensive. Keep in mind, however, although more detailed policies can potentially induce greater savings, longer policies can be more complex and generate employee resentment.

Corporate culture and company philosophy are key considerations when developing spending policies. Some companies may prefer to explicitly spell everything out, while others may chose to build a framework and add to it as the need arises.

Before digging into the granular details of the policies, take time to gain an understanding of how employees are currently spending money. Ask questions about how spending is happening now.

For example, learn how employees are buying office supplies. Do they make purchases online with personal credit cards, and then submit the charges on expense reports? For company travelers, who books what kind of car, hotel, airline ticket and how are they purchased? Does it appear that numerous personal items are showing up on expense reports? Answers to these and other similar questions will provide guidance into the level of detail needed to control a particular spend within a company.

One other important consideration brings to mind many of the clichés that abound about being penny wise and pound foolish. In an effort to lower expenses, be careful not to compromise the quality of the products or services the company delivers or degrade customer satisfaction.

GETTING DOWN TO DETAILS

With the research into company spending habits and visibility into where problematic expenses may be occurring, the nuts and bolts of the policies can start to be developed.

Determine how much information is needed to understand the objective of a spend. For example, will employees be required to identify which prospects or clients are the focus of a travel and entertainment spend, or specify the purpose of specialized office furniture purchases in order for an item to be approved?

What is the approval hierarchy and what authority does each person have? Keep in mind, the hierarchy may be different than the organizational structure of a company. Approval amounts may be set by job function or by named individual, depending upon where they fall within an organization and/or the size of a company.

There aren't industry standards for the amount a specific title or person should approve. It will be unique to each company and is based upon what makes the most sense.

Will there be category approvers? This will be approvals required beyond the hierarchy established, such as a sign-off from the information technology department for any technology purchases or the office manager for furniture or office supplies.

Will purchases be limited to departments, business units or locations? Some companies limit spending to these specific areas within the organization. For example, only people in the marketing department can make marketing-related purchases.

Now that there is data compiled about who is spending what amount with which companies, consider creating a preferred vendor list and negotiating better rates based upon an aggregate purchase threshold. Then limit purchases to a specified list of vendors.

Determine what will and will not be reimbursed. Company culture plays a large role in how restrictive or free this list might be. Considerations include such things as alcohol consumed on the road or with prospects and clients, membership dues, conference fees, seminars, sponsorships, cell phone reimbursements, meals, and more.

Most travel expenses are reimbursed after the fact, so another consideration is whether to require pre-travel authorization or travel vouchers before a spend happens. This does require more work from employees up front, but provides a measure of control before a trip occurs.

PUTTING "TEETH" INTO POLICIES

"A budget tells us what we can't afford, but it doesn't keep us from buying it." ~William Feather

Corporate spending policies are meaningless if they are not enforced. The most effective way to engender a culture of compliance to spending rules is to make employees aware of them.

Be proactive in getting the information out. Spending policies should be updated and disseminated from one centralized source. Train employees on the new policies and post them in prominent locations online.

According to PayStream Advisors, training employees can result in 33-to-50-percent fewer policy violations. When employees know their boundaries and are rewarded through rapid reimbursement of out-of-pocket expenses, they will pay closer attention to spending policies and more readily comply.

PayStream Advisors adds that it helps if employees understand why policies exist and how deviations can impact the bottom line, especially if they share in profits in some way. Empowering employees with information will make them feel a part of the solution, rather than being restricted or deprived.

When new policies go into effect, take time to audit expense reports for compliance. This will help identify the effectiveness of the training, as well as areas and/or employees where concerns need to be addressed.

Determine how policy violations will be handled. Will over-budget purchases or expense reports be denied payment, or will they simply be flagged for managers to determine whether or not to approve the spend?

PayStream Advisors reports that enforcement in one of its larger client companies includes a call from the chief financial officer to the offending employee on the third policy violation.

Finally, make sure everyone is doing the same thing, from reporting expenses, submitting purchase requisitions or orders, and approving incoming invoices.

WHY CONSIDER AUTOMATION

Many small and midsized companies are turning to third-party systems to automate processes and approval workflows to achieve consistency in procedures and improve employee compliance to policies. This reduces the personal interaction and time it takes to enforce policies, significantly easing unnecessary burdens on the finance team.

For traveling employees, an automated system can mean faster reimbursements of out-of-pocket expenses and fewer complications submitting reports. Many systems include scanning or faxing capabilities that digitally attach receipts to the reports. Offline capabilities allow employees on-the-go to fill in reports and synch them to online systems the next time they connect to the Internet.

The cost savings for automated expense control systems in both hard and soft dollars can be considerable as well. Both PayStream Advisors and Aberdeen Group, a technology research group, report that companies can expect to reduce the cost of processing an expense report by as much as $35 per report through automation. Automating purchasing and invoice management processes can produce savings of as much as $18 for each purchase requisition or invoice that requires approval.

Automated expense controls have been used by Fortune 1,000 companies for some time. However, small and midsized businesses lagged behind for many reasons, including the large upfront costs of traditional software deployments. According to PayStream Advisors, by the end of 2006, only 10% of small and 25% of medium sized businesses had implemented an automated expense control solution compared to 40% of companies with $2 billion or more in revenue.

Now, with the advent of Software as a Service (SaaS), small and midsized businesses can afford to automate operating expense controls and are beginning to adopt this technology at a rapid pace. Aberdeen Group reports that 61% of the small and midsized companies it surveyed in 2006, plan to use or consider SaaS financial applications in the next 18 months.

Automated systems ensure end-user awareness and adherence by delivering policy as employees fill out transaction documents, such as expense reports and purchase requisitions. In essence, controls are pushed out to the end user as part of the system interface.

Because policies can be enforced at the point of spend rather than after-the-fact, the need to correct errors and retrace steps are eliminated. The end result is proactive enforcement of policies and subsequent prevention of out-of-policy spending. Control becomes defacto standard, instead of a constant concern.

Here is an example of how an automated expense reporting process might work:

Required fields are linked to spending categories, which are set up in compliance with company spending policies. As employees fill out the report, they are alerted to out-of-policy spending. An automated system allows companies to set up expense reporting categories and policies governing airfare, hotels, rental cars, meal allowances, and other

T&E categories. Categories can be further configured to set specific information fields that employees use to provide details about the nature of their expenses.

Best of breed T&E solutions allow companies to set smart flags to auto-truncate or reject amounts that exceed category limits. Employees will see out-of-policy spending as they fill out their report and will be less likely to submit a report with errors, dramatically reducing processing time. Managers in the approval chain should be able to override certain flags on a case-by-case basis. Changing user behavior via policy enforcement eliminates T&E expense waste.

These same controls can also be applied through automation to other areas of a company's operating expenses, such as purchasing and A/P invoice management.

Finance teams will find a wealth of data at their fingertips inside their automated expense control systems. The analytical capabilities enable finance departments to scrutinize spending from a wide variety of levels such as by expense, employee, department, region, business unit, company and more. This detailed information can be used to identify what is and is not working, what areas may need further clarification, or what new policies need to be created. The data can also be used to strategically acquire volume and bulk discounts from preferred vendors.

FOCUS ON THE BIG PICTURE

By establishing spending policies that encompasses all company spending, finance executives will make significant in-roads into reducing costs and improving profitability.

Automating expense control processes enable policies to be visible when spending requests are made, significantly reducing the time spent policing and enforcing employee compliance. Ultimately, this means finance teams can stay focused on the big picture and continue to develop and implement strategies for continued company growth.

Resources

How to Put The Brakes On Rising Travel Entertainment Costs
By Rich Freeman
Microsoft Midsize Business Center

Getting a Grip
Expense management is the top financial planning priority at many midsize companies
By Fawn Fitter
Microsoft Momentum, a newsletter, magazine and Website for midsize U.S. businesses

Tame Your Travel & Entertainment Cost Beast: 4 Tips
By Christopher Elliott
Microsoft Small Business Center

Travel and Business Expense Reimbursement Policy
AccountingWeb, Inc. and PolicySoft
Available for free download at http://www.accountingweb.com/marketplace/policy/

A Model Business Development Expense Reimbursement Policy for Your Firm
By Bob Weiss, April 2007
Law Practice Today

Survey: Mid-Sized Companies Beef Up Cost Control, Invest in Productivity
Tools As Economic Outlook Modifies
CFO Research Services & American Express, March 2007

Spend Management: One of the Best But Least Known ROI Stories in the Technology Industry.
TripleTree, Fourth Quarter 2005

Software as a Service Buyer's Guide: Assessing Where and How to Use SaaS Applications in the Enterprise.
AberdeenGroup, August 2006

Financial Automation Survey: P2P Benchmarking Report.
PayStream Advisors, September 2006

Travel and Expense Management Report
PayStream Advisors, June 2006

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Expensewatch.com is a complete web-based subscription service that gives small and midsized companies comprehensive tools to control and reduce operating expenses. Customers automate the control of their expenses with modules for T&E Expense Reporting, Purchasing and A/P Invoice Management. Corporate spending policies are automatically enforced and compliance issues are addressed. Budget management, real-time reporting, implementation, training, upgrades and support are all included in the subscription pricing. Expensewatch.com seamlessly integrates with most accounting, ERP and corporate systems to ensure transactional efficiency. Currently, thousands of people in more than 15 countries are using the expensewatch.com service.

1.866.399.2824
www.expensewatch.com

Expensewatch.com
1100 East Hector Street
Suite 223
Conshohocken, PA 19428

expensewatch.com™