PRGX®

TECHNOLOGY'S IMPACT ON YOUR CONTRACT COMPLIANCE PROGRAM

OVERVIEW

Financial leakage happens all too often. And given the amount and complexity of contracts today, most companies are working at warp speed, with employees taking on more and more responsibilities compared to previous years. Now more than ever technology is becoming a critical component for contract compliance professionals to do their job. While the work to perform contract compliance reviews has traditionally focused on recovering funds, there's often contention around issues that led to financial leakage in the first place. Including a preventative approach in your program, with solid controls in place, can help with not only recovery opportunities but future cost savings. Technology is one way to combat contract compliance issues and keep your company profitable in the long run.
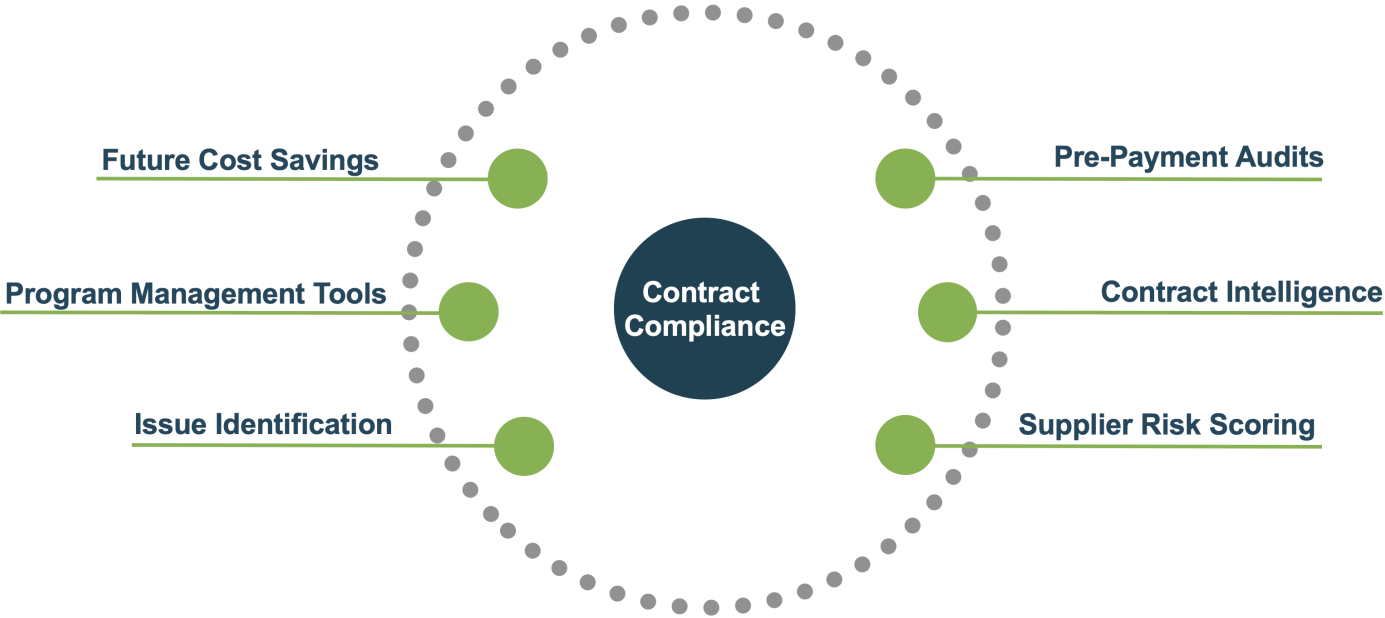
In this white paper, Technology's Impact on your Contract Compliance Program, we've identified two key concepts with supporting actions to leverage technology and expand contract compliance programs for optimal results:

- ◆ Applying Technology to Drive Coverage and Speed
  - Supplier Risk Scoring
  - Program Management Tools
  - Issue Identification
  - Pre-Payment Audit
- ◆ Key Areas of Technology Application
  - Determining the Focus
  - Executing the Work
  - Managing the Effort

APPLYING TECHNOLOGY TO DRIVE COVERAGE AND SPEED

Technology is changing the contract compliance landscape and allowing companies to uncover financial leakage more efficiently than before. But when it comes to future cost savings, putting controls in place to stop leakage before it happens is equally if not more important.

Companies are faced with a lot of decisions and can find it difficult to gain the internal support needed to close leakage gaps. By leveraging technology, companies can gain insight into known breakdowns and predict future cost savings, bringing transparency to the amount of money they would save over a long period of time. Let's explore ways technology can be applied effectively for optimal results.

Future Cost Savings

Program Management Tools

Issue Identification

Contract Compliance

Pre-Payment Audits

Contract Intelligence

Supplier Risk Scoring

Supplier Risk Scoring

When spend (the amount of money paid for a particular purpose or over a particular period of time) is assessed on its own, it is not always a good indicator of financial risk. Leveraging technology with a contract intelligence component results in a broader review as the technology works to scan supplier contracts, flag risky commercial terms, risk rank the terms and compare to spend for a comprehensive risk score. The risk score is then used to drive targeted audit programs where a balanced risk portfolio can be achieved, with a mix of strategies to go deep and broad depending on the supplier.

Standard ERP systems aren't always able to catch errors because the data needed to run rule-based logic is more granular than what traditional solutions have access to.

Program Management Tools

These tools track not only the execution strategy, for example which audits are planned for Q1 vs Q2, but also visibility into the audit life cycle, the progress on each audit, what errors have been found and savings generated. In addition, they provide an essential repository for how companies communicate with their vendors, stakeholders and third-party audit firms – reviewing issues real-time, collaborating on the resolution strategy and tracking against key performance indicators.

Issue Identification

Oftentimes, complex or limiting terms and conditions that don't reflect what will occur operationally or routinely between parties outlined in the contract can result in issues leading to financial leakage. An example of these issues can occur when the contract is "silent" in identifying activities that drive cost.

For audit teams, documentation of issues is an area that has been technology driven from the start. Originally captured in Excel spreadsheets and Access databases, more sophisticated solutions have come in the last decade or so with rule-based logic capabilities that offer a granular approach to programmatically identifying and classifying issues. The ultimate goal is to identify, resolve and put a plan in place to prevent issues from occurring again.

As a result, this allows advanced technology solutions to find issues faster, create transparency and quickly address problem areas saving companies hundreds of thousands of dollars.

Pre-Payment Audit

Layering the rules logic from issue identification on top of the invoices you process, technology can then be used to automate error review and breakdowns using the invoice line item details before money ever goes out the door.

Pre-payment audits have seen a recent uptick in leveraging contract intelligence technology where audit tools can churn through hundreds or thousands of contracts and identify risky commercial terms. The commercial terms are then turned into rules that leverage artificial intelligence to further train issue identification software to zero in on not only routine errors, but also risky commercial terms that are common across suppliers. Contract intelligence not only empowers third-party audit pre-payment solutions, it also helps effectively design audit programs by identifying the suppliers and approach to focus the efforts.

What is artificial intelligence?

In computer science, artificial intelligence, sometimes called machine intelligence, is intelligence demonstrated by machines, in contrast to the natural intelligence displayed by humans and animals.

Complexity
Terms, Conditions
& Intent

MEDIUM RISK
High Complex / Moderate Spend

HIGHER RISK
High Complex / High Spend

LOWER RISK
Moderate Complex / Moderate Spend

MEDIUM RISK
Moderate Complex / High Spend

Spend

KEY AREAS OF TECHNOLOGY APPLICATION

Determining the Focus: Targeting Financial Risk

Complexity and spend come together to determine financial risk. When reviewing the many contracts a company may have, it's important that the third-party audit services provider stratify them into buckets. This is done by applying the technology to pick out specific key words or phrases within the contract universe. The large contract universe is then parsed out into the identifiable buckets, especially the buckets of contracts that may be deemed worthy of review.

This stratification uses technology to identify opportunities around risk and complexity. You can use technology not only to assess risk but also to prioritize them into the different risk bands. This approach enables companies to work with their audit services provider to customize how they approach their audit programs.

Determining the Focus: Program Setup

Based on the risk profile of the supplier and where their risk score lies, it may make sense to go more in depth. This could mean having the third-party auditors onsite to see first-hand if commercial terms are being adhered to or if breakdowns exist. In those riskier situations, it may require doing a deep dive into the invoice details, the supporting timesheets and equipment logs which would entail running it all through risk identification technology at the deepest level to identify risk and possibly even systemic breakdowns.

This kind of in-depth review has an associated cost - the cost of having the outside audit team onsite and the amount of time involved in the level of review. As a result, not all suppliers may be candidates. In order to meet the coverage targets, moderate or lower risk suppliers in the risk assessment process may require broader reviews, running them through routine price checks and/or contract diagnostic reviews. This allows teams to identify if contract language needs improvement or if pricing errors are uncovered without sacrificing coverage and minimizing costs.

In the end a lot goes into identifying the desired risk balance and how to optimally set up a contract compliance audit program.

Assess Risks

Prioritize

Customize Approach

Minimize Costs　　**Maximize Value**

Increase contract coverage

Expand depth on risky suppliers

Executing the Work: Reach Wider and Dig Deeper

When technology is in play, it's important to understand how it can be applied. Below are elements audit experts should have in place:

- Contract intelligence – drives the risk assessment and test-building process, as well as empowers the contract diagnostic process in identifying process improvements in contract language.
- Online collaboration tools – works directly with vendors to acquire the data and documentation needed to execute the audits.
- Risk identification tools – empowers audit teams to efficiently and effectively identify errors, including systemic breakdowns across suppliers using the same contract language or systems.
- Technology aided issue resolution – allows vendors to review issues, respond directly and companies can review the responses and make determinations on how to proceed, moving to settlement quicker.

One concept to execution is "reaching wider." One method of reaching wider includes the contract intelligence software's ability to turn contract rate sheets and commercial terms into rules that can then be applied against each of the supplier invoices on a line item basis. This is done by using artificial intelligence to run error checks whether in pre-payment or post-payment implementation. Once errors are identified they can be taken through sophisticated workflow processes to handle error routing, whether for autocorrect, human review, or back to the suppliers to make the corrections and then resubmit. The power of reaching wider not only increases the coverage but also when applied to pre-payment can mean immediate savings.

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By leveraging a mix of technology approaches, companies can put together their execution plan. Even with technology and automation, complex contracts or environments require onsite or hands-on evaluation by audit experts (sometimes third-party entities) trained in ensuring contract compliance and financial controls are in place."

Field Expertise

Contract Intelligence

Collaboration

Risk Identification

Issue Resolution

Historically, contract reviews are completed by a manual process that focuses on the most complex relationships. Without technology the work has been limited because it was too much for companies to take on. The game has now changed, and while technology is at the forefront, a manual process is still needed to enable the application of technology. Once technology is applied auditors can move more quickly not only on broad review audit types but also on a deeper level. The best way to do that on a complex agreement is to bring audit teams in to conduct deep dives that includes reviewing many moving parts and components that drive cost for businesses. These audits require a lot of customization and testing, including manual reviews of backup support and interviews. After completing the first audit exercise, the complexities within the agreement are understood and can limit the need for manual audit tests in the future. Many audit tests can be automated utilizing technology going forward.

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Managing the Effort: Tracking and Reporting

Contract compliance audits have a slightly different workflow and life cycle than traditional accounts payable audits, and companies routinely express how hard it is to find solutions that meet their unique needs. Over the years, solutions have evolved to become more robust with online capabilities and sophisticated web tools. These tools provide a central repository for storing contract specifics and audit documentation like errors identified for each vendor. This makes a wealth of information immediately available to companies including vendor data and spend types, occurrences of leakage and what contract information needs to be addressed. The ultimate goal is to help capture management points and ways to prevent profit loss.

With future cost savings associated with these corrective actions, there is also transparency into how much savings could be realized by making contract or other system adjustments not just for analysis but also for tracking resolution. Program management systems really empower users with on-demand reporting that allows members of the organization to have quick access to audit progress, the impediments, savings to date, and what to tackle next.

Managing breakdowns that are identified from start to finish can have an intricate workflow process. As a company, you may need to review certain issues, and others, you defer approval to your audit team. In those cases, complex rules can be setup for issue routing.

Program management tools are an important and powerful method that when implemented will help you stay on top of the effort and make sure it's focused on your company's goals.

SUMMARY

WHERE DO WE GO FROM HERE?

Financial leakage won't dry up anytime soon. It's the nature of business and will continue to occur if companies resist changing their mindset and ways of doing things. Leveraging technology is the key to identifying the cause of leakage and resolving those issues, as well as understanding what needs to be done to help prevent it from occurring again. In addition, the thought process must shift from a post-payment cash recovery to a mindset of prevention. This is where technology offers opportunities for wider scale audit programs, better program management and a forward-thinking model that procurement professionals aim for.

Now is the time to start transforming your contract compliance program! Below is a summary of actionable steps you can take to get the most out of your compliance audit program:

- Focus on technology-enabled solutions. Technology empowers teams to identify risks faster and resolve them quicker.
- Incorporate artificial intelligence and machine learning into the technology platform to enable more opportunity to maximize program value.
- Create sophisticated contract engines to drive targeted vendor selection.
- Seek out solutions with built-in collaboration components to strengthen company supplier relationships.

Consider your options for getting the professional guidance needed to help you achieve your goals. PRGX is on the cutting edge of development with many of these emerging trends and ready to partner with companies to perform contract compliance audits and help realize the power of technology and prevention.

PRGX® | See What You've Been Missing™