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JOC Freight Payment Benchmark Study

Driving Strategic Value Through Outsourcing

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Introduction

Understanding the freight audit and payment industry has historically been an elusive exercise. That's due to a paucity of information about variations in audit and payment strategy between international and domestic shippers; how different shippers calculate their costs to process invoices; the degree to which shippers turn to outsourced audit and payment vendors; and on what basis shippers are making those outsourcing decisions.

The Journal of Commerce's inaugural Freight Payment Benchmark Study, "Driving Strategic Value Through Outsourcing," is designed to provide clarity into some of those opaque market dimensions, helping shippers determine where they stand among their peers in handling this critical, but often overlooked, logistics function.

The report is based on survey responses from 77 shippers across all major freight modes, with roughly three-quarters of them belonging to organizations with $1 billion or more in annual revenue. Thus, this study represents perspective from shippers accounting for billions of dollars in annual freight spend.

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Section I: The Outsourcing Divide

A simple dividing line that underscores how shippers manage freight audit and payment is whether they outsource a portion of that process to third-party vendors, commonly known as freight audit and payment (FAP) providers. It may seem a simplistic metric, but it's actually a key insight into how a shipper views the payment of invoices. Is it a core internal responsibility, a burden that can be offloaded for efficiency or cost savings, or a driver of insight into carrier relationships and other logistics performance areas?

Nearly two-thirds of respondents said they've outsourced either audit or payment processes — if not both — and that group skews heavily toward larger shippers that have more carriers and individual invoices to manage (see Fig. 1).

Whether or not they outsource the freight payment function, shippers can look to the data collected in those processes to guide strategic decisions and analytics initiatives. Among the potential benefits of viewing audit and payment as more than just a rote financial function, respondents focused mostly on how it could inform financial decisions, like carrier negotiations and freight spend reductions (see Fig. 2). Third-party vendors are geared to drive those insights, and shippers handling audit and payment in-house need to develop proprietary systems and processes to carve out similar benefits.

Fig. 1 Payment and Audit Outsourcing Decisions

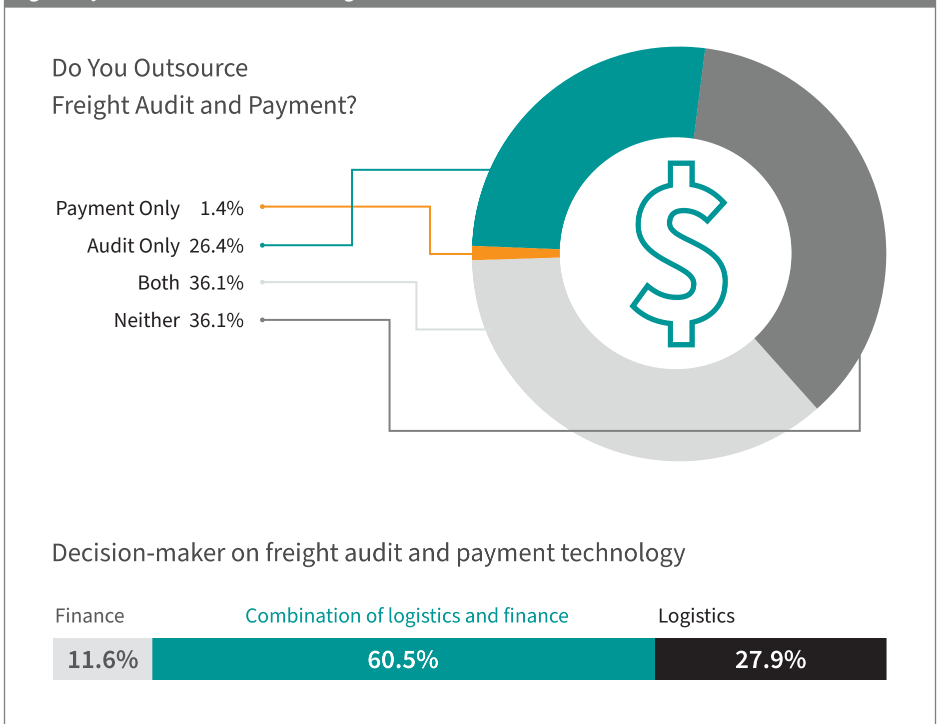
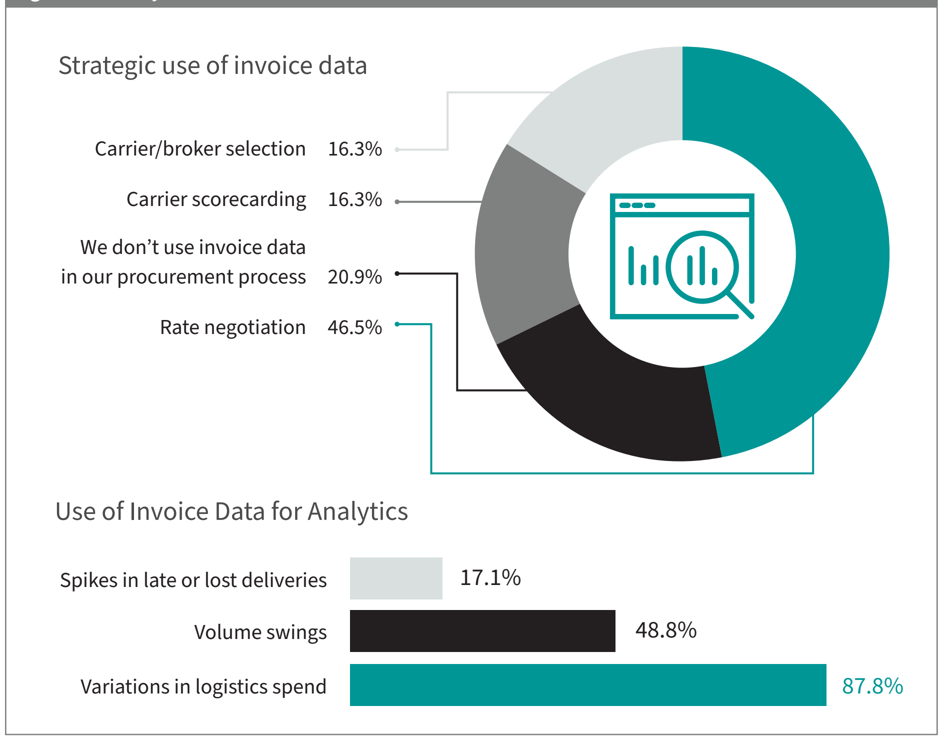


Fig. 2 Use of Payment Data



Section II: The Invoice Processing Burden

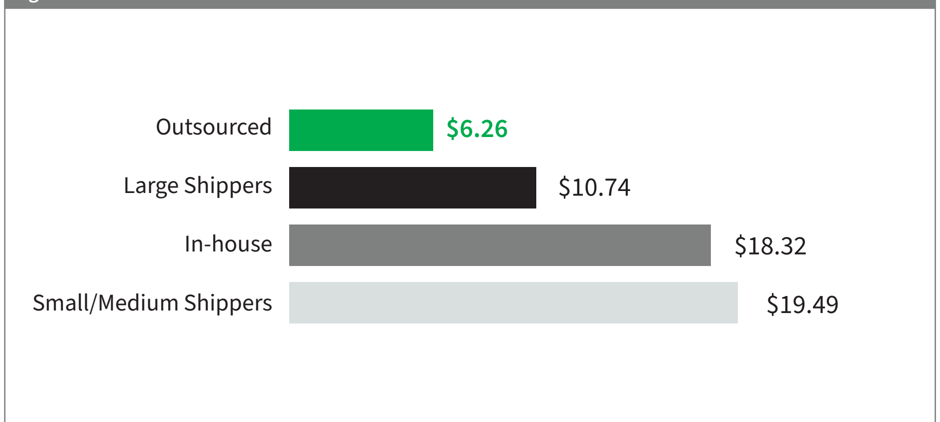
The holy grail of FAP metrics is determining the cost to process an invoice. While refining the process to audit and pay freight bills can yield adjacent benefits such as those highlighted in Fig. 2, the core of the value of such an approach is still tied to reducing administrative costs, increasing invoice accuracy, and avoiding overpayment.

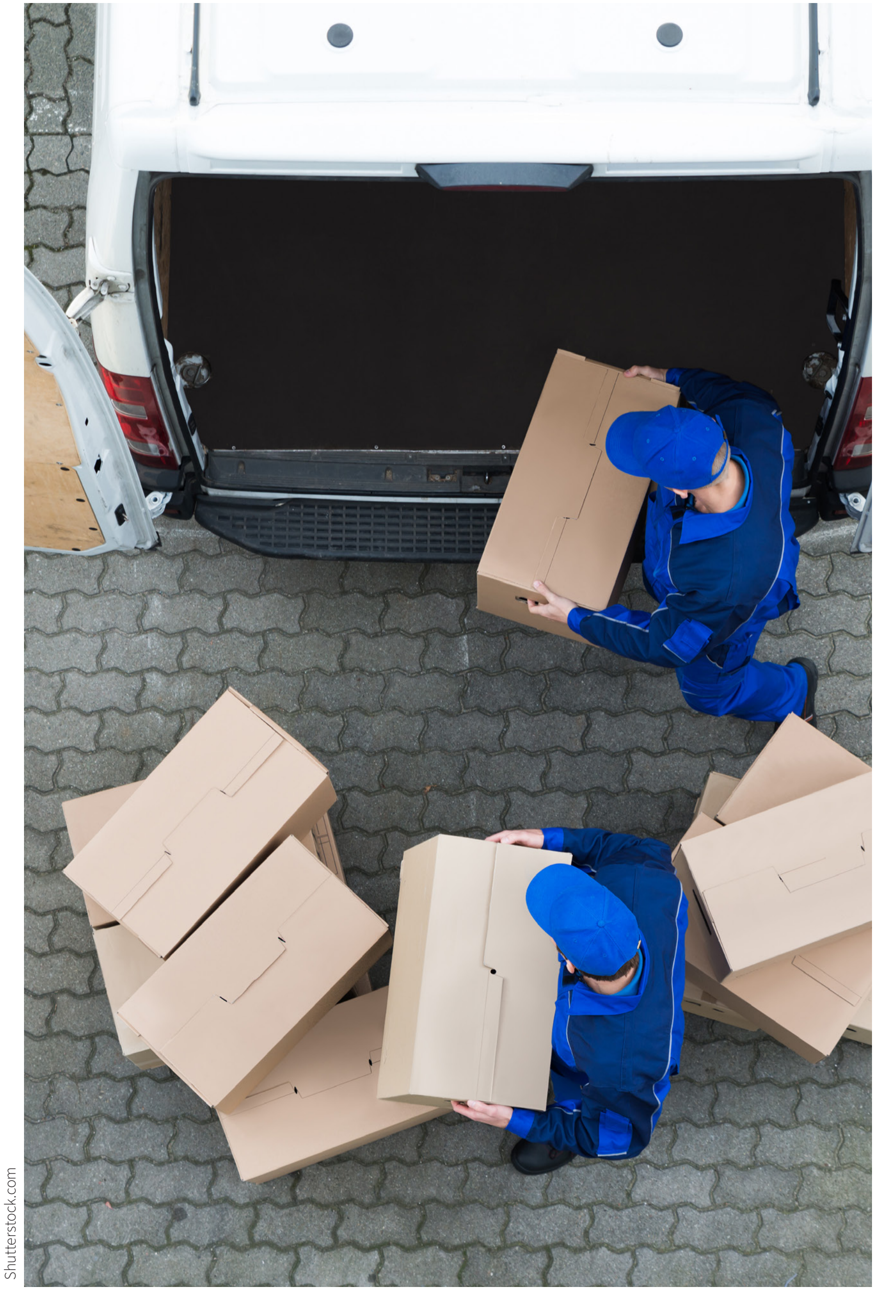
Consider a shipper with $1 billion in sales. Using a common industry estimate of freight spend representing 5 to 10 percent of total revenue for a shipper, that would equate to $50 million to $100 million in freight spend. If we assume an average invoice of $2,500 across modes, that's roughly 40,000 invoices over the course of the year.

If that shipper can reduce the cost to process each invoice (whether internally or to a vendor) from $20 to $10, its total annual administrative costs would drop from $800,000 to $400,000.

According to survey respondents, large shippers, which are more likely to outsource some aspect of audit and payment, have invoice processing costs nearly half those of small shippers (see Fig. 3). And those outsourcing some or all of the audit and payment function report average per invoice costs that are roughly one-third of those reported by shippers handling the process internally.

Fig. 3 Cost to Process an Invoice





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Section III: History Tends to Repeat Itself

Among shippers that outsource their freight payment and audit processes, a secondary divide has emerged between bank-backed payment vendors, some of whom also offer audit services or partner with audit firms, and non-bank-backed vendors.

To be clear, all companies involved in paying bills on behalf of customers have a fiduciary responsibility to their clients. Bank-backed vendors, however, note that they have the advantage of being regulated in a way that non-bank competitors are not.

This is no new phenomenon, but is the industry in 2020 any more conscious of that bank-backed or non-bank-backed fork in the road?

More than 60 percent of respondents using a third party vendor use a non-bank-backed one, while only a quarter think it's important to use a bank-backed one, and only 15 percent say historical bankruptcies of non-bank-backed vendors influenced their decision to use a bank-backed one (Fig. 4).

There is broader general awareness around system vulnerabilities to threats across all categories of software, and that was manifested in mid-2020 when a major FAP vendor was hit by a days-long systems outage.

Despite that, most shippers responding to the survey said they were at least somewhat confident in their provider's system security. But only a quarter were very confident (Fig. 5).

Fig. 5 Confidence in System Security of Payment/Audit Vendor

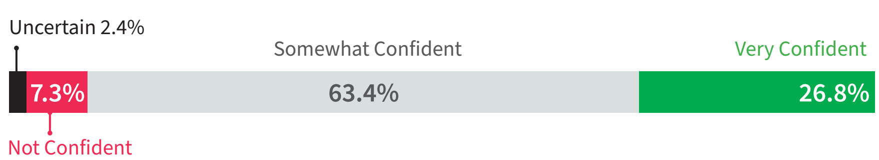
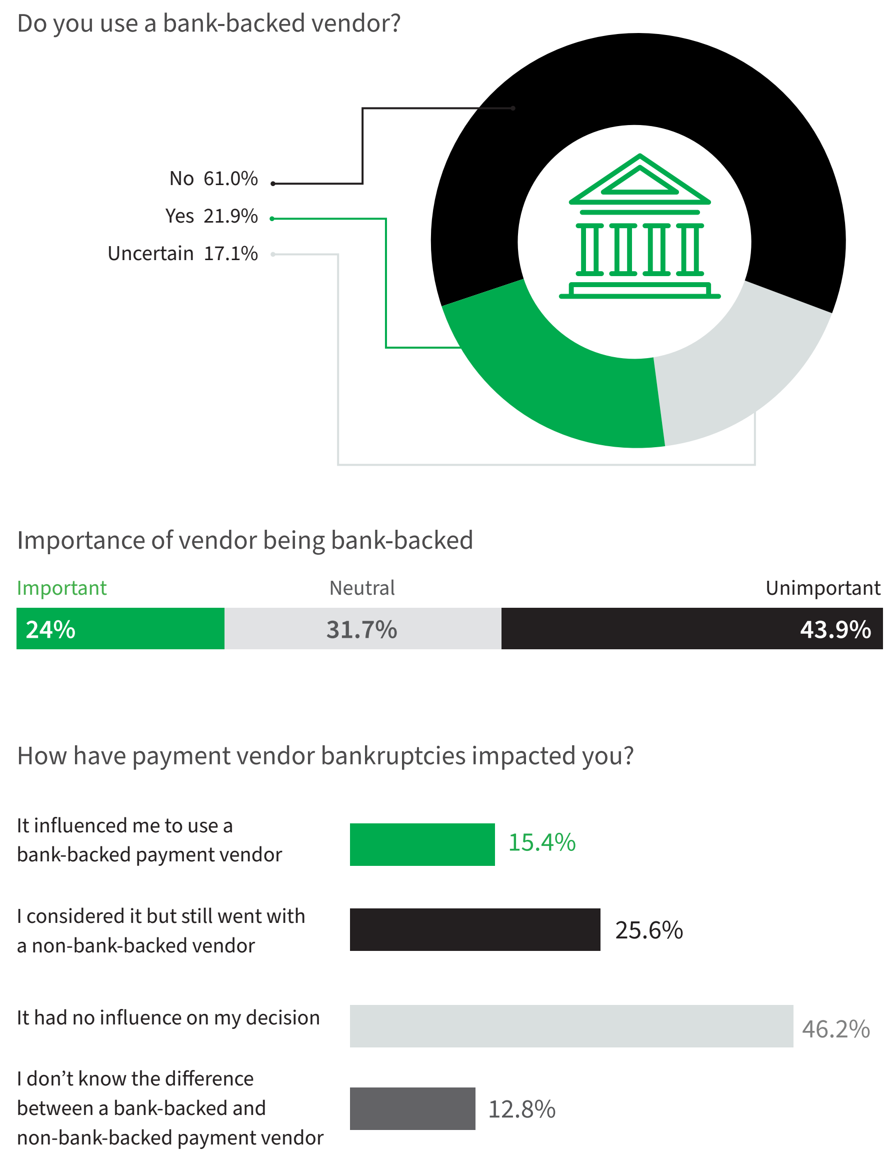


Fig. 4 Perspective on Bank-Backed Vendors



Section IV: The Payment Terms Conundrum

The bookend to the audit and payment process is the procurement process, and a core part of that function is related to payment terms, the amount of time between a service being rendered and when the bill associated with that service is due.

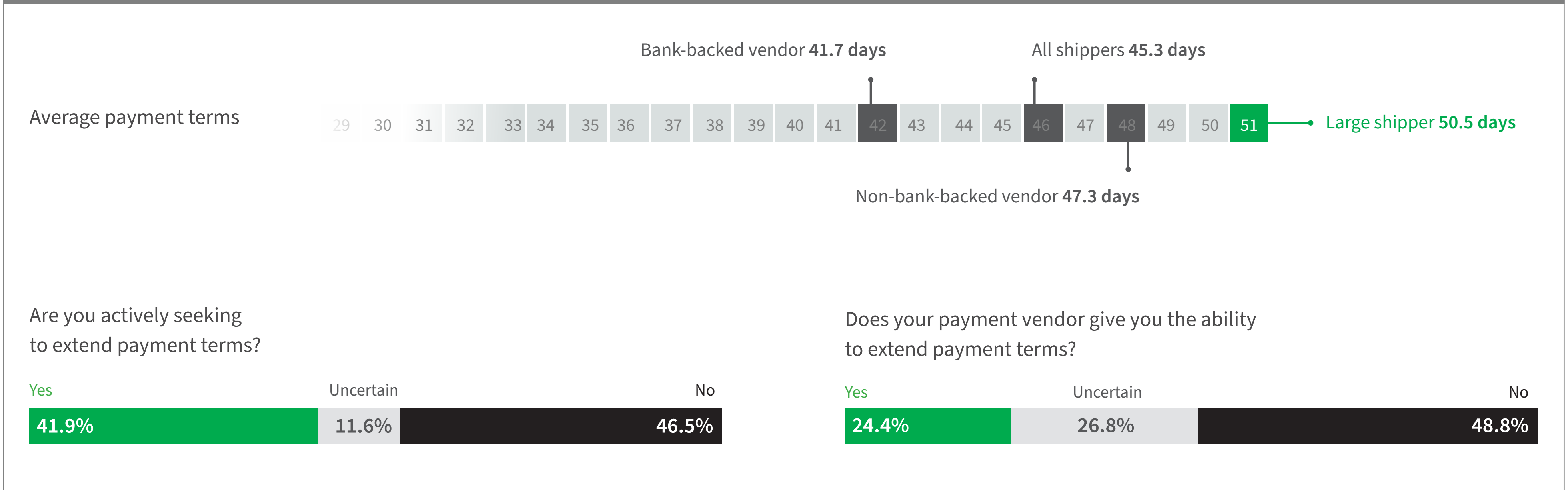
Payment terms for shippers to their carriers varies widely, from just 15 days to as long as four months or more, according to survey respondents, depending on the mode, the relationship between the parties, the volume a shipper commits to a carrier, and more near-term dynamics like the state of supply and demand in the market.

In general, shippers aim to extend their payment terms with carriers without upsetting those relationships in such a way that it would disadvantage them. Modern payment processes revolve less around theoretical “win-win” scenarios than they do about pragmatic compromises. When a third-party vendor is involved, financing technology products can be used to help find that common ground.

Survey responses show that larger shippers tend to have longer payment terms than their small and medium-sized counterparts (see Fig. 5), which makes sense given that shippers with larger volumes tend to have more leverage with carriers. Those respondents using bank-backed vendors also reported shorter payment terms than those using non-bank-backed solutions. Companies using bank-backed solutions typically lean on those vendors to extend their days payable outstanding (DPO) while getting their carriers paid according to the terms of the contract, if not earlier.

Only 42 percent of respondents say they are actively pursuing longer payment terms with their carriers, a clear sign of the inseparability of payment terms from the larger shipper-carrier relationship.

Fig. 6 Payment Terms



Section V: Takeaways

- Shippers that outsource some or all of their audit and payment process pay drastically lower per-invoice costs than those that handle everything internally;
- Shippers reported an average invoice inaccuracy rate across all modes of 20.8 percent;
- Nearly 80 percent of shippers say they are invoiced for parcel moves alongside other modes, a substantial increase over previous industry estimates, which hovered in the 60 percent range as recently as 2017;
- Shippers using bank-backed FAP vendors can avoid having to negotiate longer payment terms with their carriers due to access to financial products that extend their days payable outstanding;
- Despite the disruption caused by the coronavirus disease 2019 (COVID-19), fewer than 10 percent of respondents say the pandemic will make them change the nature of their existing outsourced freight audit and payment relationships;
- Larger shippers are more likely to outsource some component of the audit or payment process, have access to products that provide longer payment terms, and pay roughly half the processing costs per invoice than their smaller peers;
- And the primary uses for payment data are tied to arming shippers with better analytics for rate negotiations and for reducing freight spend.

Methodology

This study was based on an anonymous survey of 77 international and domestic cargo shippers that are invoiced for various modes of global and domestic freight transportation. Responses were collected from early July through mid-August 2020 (Figs. 7 &8). Analysis of the data was conducted solely by *The Journal of Commerce.*

Fig. 7 Survey Demographic

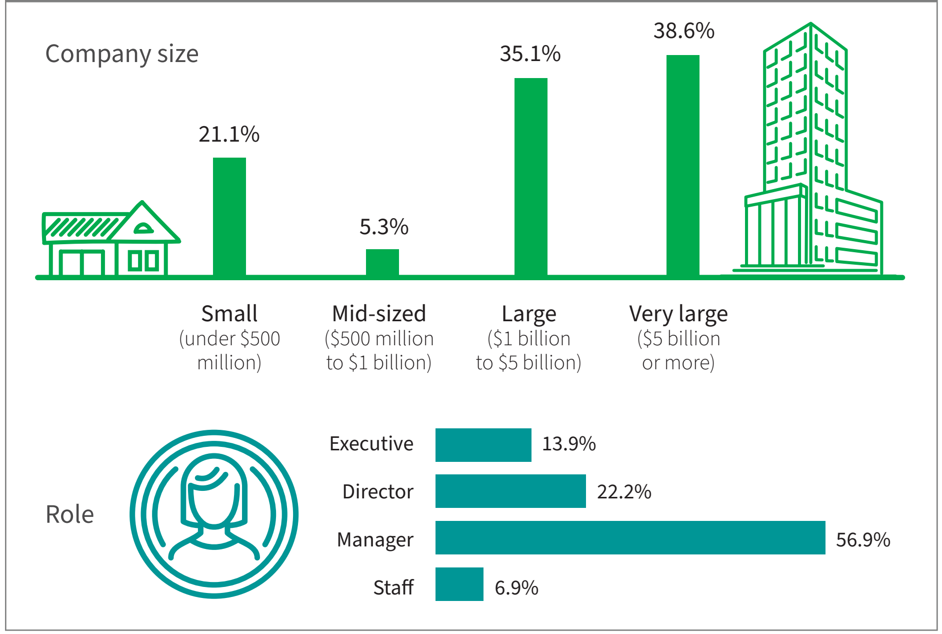
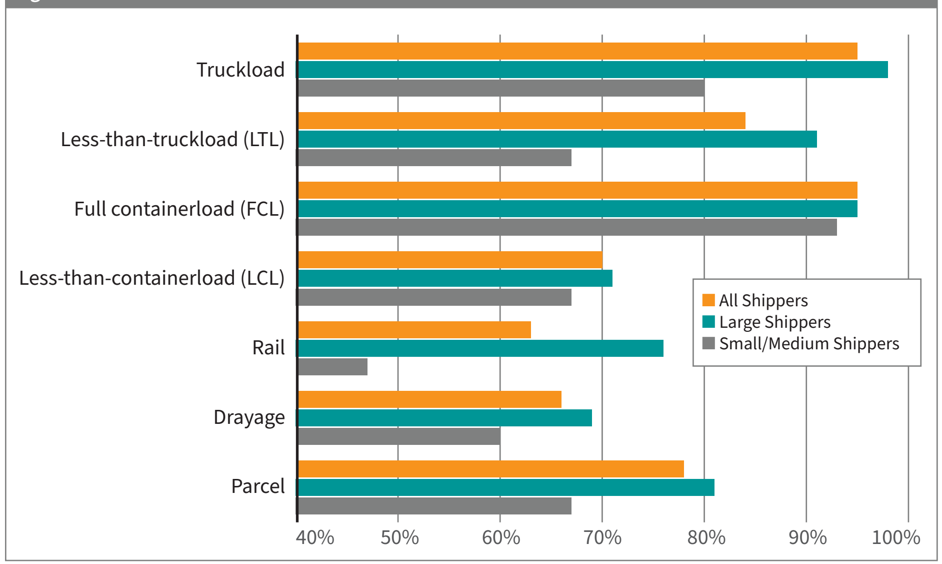


Fig. 8 Invoiced Modes



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