

Historical Telecom Audit Is Still a Valuable Function

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Enterprises that are not auditing their telecommunications invoices are forfeiting an extra 10% or more of their network services spending to the network service providers (NSPs). Historical audits recover overpayment, identify stranded assets and increase budget efficiency.

Key Findings

- Historical audits are decreasing as a stand-alone service and are now bundled as part of a broader telecom expense management solution.
- Contingency fee pricing is a function of governance but should not exceed 50%.

Recommendations

- Remove limitations clauses from network service contracts. Limitations clauses reduce the amount of time that invoice discrepancies may be disputed.
- Only submit payments to the auditor once the refunds have been recovered and discrepancies have been corrected and confirmed via subsequent invoices.
- Perform a historical audit at the onset of deploying telecom expense management (TEM) services and use them to benchmark the effectiveness of your TEM vendor.
- Formulate and execute a strategy to increase the level of the enterprise's telecom governance.

WHAT YOU NEED TO KNOW

Carrier invoices are not accurate and will become even more inaccurate with the continued consolidation of carrier billing systems. Enterprises that do not possess the skilled staff to audit telecom invoices are overpaying and must recover those payments. Hiring a third-party consultant to perform a historical audit will recapture these overpayments and enable them to be placed directly back into the budget, less the consultancy fee.

ANALYSIS

Enterprises are challenged with the auditing of their telecommunications invoices (paper and electronic) and reconciling network inventories. The challenge is due to the lack of resources and staff understanding of telecommunication services terms and conditions and of billing formats. The result has been overpayments, stranded assets and the inability to effectively manage the telecom expenditures. Implementing a historical audit through a consulting arrangement will identify discrepancies, identify stranded assets and recover the overpayments.

Historical Audit Overview

Historical telecommunications audit services have been performed for decades, and the trend was to perform a telecom audit every one to five years. In the past, telecom invoices were only paper-structured and were labor-intensive to audit, so contingency-based audits from third-party specialists were most often structured at a 50% contingency fee for recovered funds. Enterprises were willing to relinquish half of their recoveries to consultants because half was better than no return at all. However, further reductions in their savings were restricted because many vendors had the overaggressive practice of attaching "ongoing or future" savings fees for long periods of time or until the expiration of the network service contract.

Today, billing error rates are increasing due to the consolidation of carrier billing systems and the more complex class-of-service data services; however, the value of the adjustments is actually decreasing. At the same time, the number of enterprise network services bills, line items and elements within the line item have increased, thereby creating more auditing items. All of this does not equate to a lesser savings potential but rather extra diligence required in the invoice auditing process.

Historical telecom audits are still offered; however, they are rarely marketed as a stand-alone service but rather as an underpinning and adjunct function to a broader solution. Enterprises tend to have audits performed on a more frequent basis (one to three years), and contingency rates, although very important, vary as the market has evolved from a standard "one size fits all" service offering to a value-added relationship based on cost reduction potential (CRP). Consultants performing telecom audits extract a great deal of information and understanding from the audit and, therefore, are able to leverage other value-based services, such as network services optimization, network contract evaluations, inventory characterizations and other TEM functions. Although there are many different services and functions that may be performed, historical audits alone still exhibit an excellent means for immediately adding funds back into the budget.

What Are the Elements of a Historical Audit?

Historical audits leverage the use of auditing software and require skilled professionals with applicable telecom and financial skill sets. They consist of auditing telecommunications invoices (paper, CD and electronic data interchange [EDI]) and customer service records (CSRs) for voice, data, long-distance, local and wireless services. Paper bills and CDs are of summary detail

and do not provide the Universal Service Order Code (USOC)-level detail that EDI invoicing or the CSRs are capable of providing. For example, there may be one billing line item; however, within that charge, there are multiple elements such as dial tone, taxes, line maintenance, call features/functions, and so on. Without this detail, only summary details will be audited. Many enterprises are still receiving their bills in paper format and, in order to do an audit to the USOC level, the consultants will have to obtain the CSRs from the carrier(s). At the onset of a historical audit, enterprises will need to sign a letter of agency that will allow the consultants to act on the behalf of the enterprise when interacting with the carriers. This enables them to obtain records, invoke disputes and manage changes, among others.

Inventory tracking will be performed, but the level and degree of physical confirmation will vary by enterprise need, the vendor's offering and what is finally negotiated. Dial tests for inventory assessments are generally included, and many auditors will include certain on-site validations, but this must be mutually agreed on by both parties. Large or complex on-site validations will increase the contingency rate, but detailed circuit inventories are a separate service and have a time-and-materials fee structure.

Once all the necessary information has been gathered, the audit will check for billing errors and discrepancies, which typically include:

- Continued charges for discontinued services
- Contracted rates applied incorrectly
- Erroneous surcharges
- Incorrect taxes
- Service installs/disconnects not performed
- Slamming/cramming (changing services without permission/adding charges to the bill for services that were not ordered)

Optimization offerings are inherent to most auditing contracts and provide the opportunity for enterprises to recognize additional savings by implementing the recommendations presented by the consultant. Enterprises that do not possess the resources to proactively manage network services assets will see additional CRP but must be certain to obtain return on investment (ROI) guarantees from the vendor.

The consultant is responsible for recovering the overpayments from the NSPs, confirming that the inaccuracies have been fixed and providing detailed reports and progress updates. Vendor payments must not be relinquished until the refunds are actually received and there is proof that the discrepancy has been changed by the NSP, such as a current NSP invoice showing the change.

What Are the Pricing Models?

There are three models offered in the market today: fixed fee, hourly and contingency.

- Fixed-fee/fixed-time is based on the consultant's analysis of how much time and effort will be required, although there is no incentive for the vendor to perform a quality audit.
- Hourly fees (commonly \$250 per hour) have the downside of the difficulty in monitoring the time spent on the audit. Some consultants may offer an option between hourly and contingency-based fees. For example, the lesser of a 30% contingency fee or x times the hourly cost. This type of arrangement may be beneficial to the enterprise, with the

worst-case scenario of just paying the contingency fee. Consultants doing high-level audits and not auditing to the USOC level may offer this option, but again there is no incentive for them to perform a quality audit.

- Contingency-based consulting is the most widely offered project structure for historical telecom audits. The fee is based on a percentage of the recovered funds. Fees today range between 15% and 50% of the reimbursement, with the lower range offered to large enterprises spending greater than \$50 million per year that have not performed a recent audit (more than a year), that have a low telecom governance and/or when the audit is bundled with a broader TEM solution. The higher contingency rates are applicable to enterprises spending less than \$25 million per year and possessing a high telecom governance. Enterprises that are acquiring the service as a means to benchmark or audit their TEM provider will most likely exceed a 50% contingency rate and/or be charged a fixed-fee or hourly rate.

Future or ongoing fees may be applied over a period of time (x amount of months) for future savings being recognized by the invoice corrections. For example, a discrepancy is identified and corrected by the vendor and the contingency fee is applied on a forward-going basis. Large enterprises (\$25 million or more in annual telecom spending) have been successful in negotiating future contingencies out of their contracts when in a competitive situation or when obtaining additional services from the vendor. If ongoing fees are present and competitive leverage does not exist, enterprises must not exceed paying forward for more than six to 12 months and certainly not beyond the term of the NSP contract.

Optimization is a value-added service and fees are generally structured at the same contingency rate as the audit. The fee is also forward based and should not exceed 12 months.

Historical audit fees will vary according to the enterprise's network services spending, number of invoices to be audited, level of corporate telecom governance, time period in which a formal audit was last conducted, the required level of audit and whether they are bundled into a larger solution. Although there are variables, the maximum contingency fee an enterprise should pay is 50%. It is these same variables and circumstances that will dictate the time it will take for an audit to be performed; however, on average, audits can generally be executed in three to six months.

Who Are the Vendors?

Telecommunication Auditors/Consultants

Traditional telecom auditors and consultants offer these services, and most will invariably propose the audit as a subset to a larger engagement but will still perform audits as a stand-alone service. Many of these vendors were established by past NSP employees who are very familiar with carrier billing and possess both the telecommunications and finance skill sets required for audits.

TEM Vendors

For TEM services to reach the highest level of cost savings and generate an ROI greater than 100% in Year 1, enterprises will require a historical audit and have a network characterization performed. The TEM landscape is a diverse set of vendors evolving from varying markets (see "MarketScope for Telecom Expense Management, Worldwide, 2H07"), and most offer audits as a service whether performed in-house or through a partner. TEM vendors focus on providing a portfolio of services to construct an end-to-end telecom life cycle management plan, of which telecom auditing is piece but may not necessarily be their core strength.

Gartner is currently not tracking or ranking the specific auditors/consultants for historical audits, simply because there are hundreds in North America. However, we can note firms, and applicable TEM vendors, that have been highlighted most often in Gartner client discussions: These are: Fortune Consulting; Levine, Blaszak, Block & Boothby (LB3/TC2); Mass-Tel Communications; PRG-Schultz; ProfiTel Group; TELAdjust; Telwares; Union Square Associates (acquired by MDSL); VGS Associates (tax and surcharge recovery focused); and the network outsourcing vendors that leverage internal capabilities and partnerships, such as Accenture, CSC and IBM.

Vendor Differentiation

Carefully inspect the vendors' capabilities when evaluating their offerings. Many vendors in the market today performing historical audits offer a broad solution set, but it is for this explicit function that they must be evaluated. There are vendors more focused on leveraging their core competencies and, although they offer audits, they do so by auditing summary detail and only recovering the large discrepancies — the "low-hanging fruit." The goal of an audit is to recover overpayments but also to have every invoice and invoice item audited. This can only be accomplished if the vendor is able to audit to the USOC level and, although the cost recapture at USOC level may not be substantial, it has its rewards from a network service element characterization necessary for compliance — especially for financial services relative to Sarbanes-Oxley.

Enterprises should not sign telecommunications contracts that contain limitations clauses that affect the time in which an enterprise is able to recover discrepancies. However, if such clauses are currently present in contracts and large sums of money are involved, vendors with telecom auditing expertise will still be able to recover some of the overpayments, although it will take more time for recovery and drive a higher fee.

Cost Reduction Potential

There are multiple reasons for performing historical audits, but the degree of return will vary according to the enterprise's specific telecom environment and circumstances. Immediate savings are recognized by the recovered funds, and future savings are gained by correcting the billing errors. Immediate and future savings added together will equal the overall CRP. Below is a guideline showing various enterprise situation levels and a CRP model to determine the amount of savings that can be expected.

High CRP

- Do not possess current resources or skill sets to audit telecom invoices
- Lack a strong governance and change management structure
- Have not engaged in a historical audit in more than two years and have not invested in TEM practices
- Have made significant changes to services and locations in the past three years
- When adopting TEM services (enterprises will recognize reduced fees when bundled into a broader solution)

Moderate CRP

- Engage in annual or biannual audits
- Have acquired an internal TEM application but are performing invoice audits internally

Low CRP

- Perform regular audits on a monthly or annual basis
- Have partnered with a TEM service provider for invoice management/audit service

CRP Model

This CRP model (see Table 1) is based on the following:

- Enterprises are spending \$10 million or more annually for network services.
- Governance levels are established by how many invoices are audited, and how often.
- Percentages reflect recovered funds from the audit and associated first-year savings recognized from the corrections.

Table 1. Gartner's CRP Model

Governan ce	Audit Each Year	Audit One to Three Years	Audit More Than Three Years
High	3% or Less	5% to 8%	6% to 12%
Medium	3% to 5%	8% to 12%	12% to 18%
Low	5% to 7%	12% to 15%	18% to 23%

Source: Gartner (July 2008)

Best Practices for a Quality Audit

- Outline a specific statement of work and insist that all invoices be audited.
- Always prepare a formal RFP.
- Select independent consultants who are not reselling networking services.
- Audit to the USOC level to provide a detailed depiction of all elements.
- Do not allow ongoing fees to exceed 12 months or beyond the term of the NSP contract.
- Assess the accuracy of the enterprise's current network assets and inventories.
- Prior to signing a contract, negotiate what level of on-site inspection will be included and the cost for additional sites.

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