

## **The Four Pillars of Modern Procurement for SMB: Giving Procurement the Whole Enchilada**

While procurement platforms are now in use to some degree in about half of Fortune 500 / Global 3000 companies, in the SMB market, procurement platforms have not yet crossed the chasm. Only true Procurement innovators in the SMB market have adopted modern Procurement platforms, which amounts to a dismal penetration rate of about 10%.

Why such a low adoption rate? There are a number of theories, and reasons, given by analyst firms large and small alike, but it generally boils down to the following:

- (perceived) platform availability
- (perceived) platform cost
- (perceived) platform process support
- (perceived) ease of platform use

More specifically, adoption is said to be slow because

- many SMBs, with limited market knowledge and limited research time, aren't aware that new solutions have hit the market over the last few years
- many SMBs are unaware that costs have come down considerably since the days when even a low end solution cost hundreds of thousands of dollars
- many SMBs are not aware that modern platforms have more flexible workflows that can adapt to SMB processes and not just mega-corp processes
- many SMBs are not aware that modern solutions are much easier to use than first generation platforms, incorporating many of the best features and functions of modern consumer shopping platforms

And all this is true. Adoption will not pick up until the average SMB company realizes that modern Procurement platforms are available, easy to use, process centric, and cost-effective. However, even then adoption will be slow unless the platforms offer all of the key capabilities that SMB Procurement organizations need to conduct their daily Procurement operations – capabilities that we have dubbed the four pillars of modern Procurement for SMBs.

In particular, as SMBs are short on cash, time, resources, and technical and platform support, SMBs need a solution that provides:

- one stop shopping
- closed loop Procurement
- budget support
- project management

In this paper we will not only explain what each of these core capabilities are, but also why they are required by an average SMB Procurement organization.

## **One Stop Shopping**

In a large organization it is not uncommon for Procurement to have one catalog or punch-out based solution for office supplies, MRO, and consumables; another solution for T&E (Travel & Expense management); another solution for contingent labor and services; and an ERP or MRP based solution for regular orders against contracts. When an organization has the budget and has the manpower to support multiple best-of-breed Procurement solutions, as well as the budget and manpower to integrate all of the spend into the ERP or analytics solution on a regular basis for spend and contract analysis, this is a workable solution. But when an organization has neither the manpower nor the cash to support or acquire multiple solutions, it needs a single solution that supports all of its daily Procurement needs. Otherwise, it is still doing Procurement in a disconnected fashion where some purchases go through the platform, other purchases go through the P-card, a few purchases go through the Sourcing system as one-time RFX events, and the remainder of organizational purchases are still done over the phone and fax and the only electronic record of these purchases is the invoice and the payment in the Accounts Payable (AP) system.

However, just having support for the majority of purchases an average SMB needs to make on a daily basis is not enough, because good Procurement requires more than just creating requisitions, sending out purchase orders (POs), and approving invoices. It also requires capturing spend, managing against contracts, sourcing one-time buys of considerable value, and market intelligence.

As a result, an SMB organization needs a Procurement platform that supports

- extensive extendable catalog support that supports punch-outs; vendor catalogs in , XML, and flat-file format; and buyer-defined catalogs for products and services
- requisitions and automatic purchase order creation and distribution that follow dynamic approval streams based upon the products and services being purchased, the total spend, and user limits
- T&E management that supports transportation, accommodation, and related service bookings
- P-card integration to match P-card transactions to purchases
- RFX for one-time large dollar purchases
- contract support for the definition of on-contract products, services, and preferred vendors
- 100% Procurement spend capture either in the solution or in an underlying ERP for future spend analytics

In addition, as per the introduction, the platform should be easy to use, support adaptive workflows, and capture the best features of modern Business-to-Consumer platforms that allow a user to quickly find the relevant products or services with a single search, highlight those under contract, the most cost-effective solutions not under contract, and expected delivery times. In addition, the platform should show a user the associated approval requirements to insure that a user understands the repercussions of each requisition they make.

The benefits of such a platform are considerable. According to a classic research series by AMR (now Gartner) on Reaching Sourcing Excellence, an average organization loses 30 cents to 40 cents of every dollar of negotiated savings for a variety of reasons, including, but not limited to:

- lack of knowledge about a contract
- lack of knowledge about how and when to order on-contract
- lack of knowledge about the cost of purchasing off-contract

While all of these problems are theoretically solved by a contract management platform that allows all organizational users to search for contracts, bring up the terms and conditions, and appendices that chronicle the average market price versus the contract price at the time the contract was signed, the following problems cannot be solved by a contract management platform:

- lack of knowledge about market pricing
- lack of knowledge about who to buy from if there is no contract

All a contract management system does is capture historical pricing and historical contracts. It is impossible to extract current market intelligence from a contract management system and equally impossible to extract information about suppliers not under contract. However, a one-stop-shopping platform that stores contract information solves all of these problems. Such a platform can highlight on-contract products and services, automatically direct purchase orders for the on-contract goods and services to the appropriate individuals at the right suppliers, and show the buyer the incremental cost of selecting an off-contract product or service. In addition, by integrating all catalogs from all sources, the platform can provide insights into current market pricing, identify any preferred suppliers, and identify the most cost-effective item when there is no contract in place.

## Closed Loop Procurement

A one stop shop is a great start as it will quickly reign in spending on products, services, and consumables as buyers are able to quickly find and requisition on-contract products and services to fulfill their needs, but it is not a complete solution. A one stop shop is not a complete solution as it relies on each and every buyer finding and selecting the right product, service, or consumable. If this doesn't happen, negotiated savings don't materialize. That's why the platform needs to support closed loop procurement.

What is closed loop procurement? It is an integrated process that starts with the identification of products and/or services to fulfill a need; the selection of such products in a one-stop shop; the creation of a requisition that is appropriately routed based upon the products and services selected and total dollar values; automatic creation and distribution of purchase orders upon approval; collection and matching of goods receipts to purchase orders; acceptance and matching of invoices to purchase orders; m-way matching between purchase orders, goods receipts, and invoices to make sure there are no discrepancies and that Procurement pays the proper amount and only for goods actually delivered; and that payment is made at the appropriate time according to organizational policy.

In our last section we noted a number of reasons that 30% to 40% of negotiated savings never materialize. These reasons included:

- off-contract purchases
- lack of knowledge about market pricing

However, these aren't the only reasons savings don't materialize. Other reasons:

- over-payments as a result of being billed at off-contract rates
- fraudulent payments as a result of invoices for undelivered products
- duplicate payments as a result of paying duplicate invoices
- payments for unapproved products and services
- late payments that result in interest and penalties

The only way to prevent over-payments, fraudulent payments, and duplicate payments is with a good three-way matching solution that identifies those payments and prevents them. The best way to prevent payments for unapproved products and services is to prevent purchase orders for unapproved products and services, and the best way to prevent those orders is to enforce a good requisition process that can ensure that only approved products and services are requisitioned. Furthermore, with instant visibility into the status of each invoice, and whether or not the appropriate goods have been received, payments can be made according to organizational policy and interest and penalties can be minimized. This is all possible with closed-loop procurement.

But more importantly, closed loop procurement helps to get spend under management as not only does all spend get captured, but all payments, all invoices, and associated delivery information gets captured as well. This provides a solid foundation for spend analysis and the next Sourcing cycle, which helps the organization identify opportunities, negotiate better contracts, and save year after year. That's the true value of closed loop procurement.

## **Budget Integration**

If an average Procurement practitioner is asked about the most critical functions a platform should provide, it's not likely that budget integration is going to roll off the tips of their tongues, but that's because they don't know that a platform could support this functionality. However, if you ask an average Procurement practitioner what their biggest challenges are, they'll probably say:

- time and resources,
- meeting savings targets, and/or
- staying under budget.

But how do you stay under budget if you don't know what those budgets are? This is a big problem for SMBs. While many big organizations have enterprise systems that integrate accounting, ERP, and Procurement, and make it easy for any buyer who wants to check spending against the budget to log in and do so, this is typically not the case in mid-size Procurement organizations where accounting is on a stand-alone back-office system, the ERP (with limited functionality) is only licensed to manufacturing, and Procurement is lucky to have anything at all.

As a result, without budget integration, Procurement is often left in the dark, working off of a monthly budget report that could be three weeks out of date, that does not account for approvals made in the previous month that have not yet been paid, and does not capture requisitions in the system yet to be processed.

This makes it very different for a Procurement manager to make a good decision when she or he needs to make a decision on a requisition. Is the buyer within their requisition limit? Even if they are, will an approval of the current requisition cause one or more budgets to be exceeded? If so, do additional approvers within the organization need to be consulted? And if a budget cannot be exceeded, how would an approval affect other requisitions in the system?

However, with budget integration, an approver can see what budgets are affected by a requisition; how much has been spent, approved, and requisitioned against each of the budgets; how approval of the current requisition would affect the situation; and who else needs to approve the requisition after the current approver.

Not only does budget integration help the approver, but it also helps the requisitioner. With budget integration, the approver can see, as he is building the requisition, what budgets are affected, who will need to approve the requisition, and if approval of the requisition is likely to cause a budget to be exceeded.

And this is great, but more importantly, when it's integrated with the one-stop-shopping capability, it can enforce visual guilt. Not only can a user see how much he is costing the organization when he doesn't requisition either the on-contract or most cost effective solution, but how many other people will see his failure to be budget conscious as he will see how many people will need to approve the requisition as it is being built. Budget integration not only keeps Procurement on track as it helps to ensure that an approver knows the full effect of each and every approval, but keeps buyers across the organization on track as they know that if they make a large request that is off contract, multiple individuals in different departments will see that request before it is approved.

## **Project Management**

As with budget integration, if an average Procurement practitioner is asked about the most critical functions a platform should provide, project management is not likely to roll of their tongues either as they see the platform as a tool to support a very tactical, function-oriented process that revolves around requisition, purchase order and invoice management. However, if one takes a step back, it becomes clear that each of these requisitions, purchase orders, and invoices relate to a project, and outside of Procurement, requisitioners are working towards completing tasks and projects, not towards managing purchase orders and invoices. Providing a project-oriented focus makes it easier for the average user to procure properly. As a result, a platform with a project-oriented focus increases adoption, decreases maverick spend, and gets spend under management.

Moreover, if Procurement is to be successful in its job, it has to be managed as a project. Procurement is only successful when, at a minimum:

- proper products and services are identified
- proper requisitions are created and approved
- proper purchase orders are sent and receipt acknowledged
- proper goods receipts are issued and correlated to purchase orders
- proper invoices are received and validated and matched to purchase orders
- proper payments are made at the right time
- proper analysis is performed on the integrated data at the right time

This involves identifying any relevant contracts, any preferred suppliers, any affected budgets, any stakeholders that needed to be notified or grant their approval, any damaged products or delivery discrepancies, any invoice discrepancies, any payment rules or unapplied credits, and any data that should be considered in a process or payment review. When you put this all together, this is not an isolated set of tactical tasks, but an integrated set of strategically important tasks woven together by a workflow that supports a sourcing project, a contract, a marketing endeavor, a legal need, and so on.

Moreover, many types of purchases need to be made on a regular basis, such as a new setup for a new employee, a swag bundle for an upcoming (set of) conference(s) or workshop(s), a monthly office supplies re-order, or a bi-weekly raw materials re-order for the production line. Over time, these orders represent the implementation of a sourcing project and a proper procurement platform that supports the concept of procurement project management allows these standard orders to be templates and re-ordered at the push of a button, or, if a few quantities need to change, it allows these standard orders to be placed with a few simple quantity changes and the push of a button. Moreover, as these templates are against projects, which have been pre-approved, there is no need to force each (re)order through the requisition process as long as no new items are added or no pre-approved quantities exceeded.

Even SMB Procurement needs project management, and unless it is embedded in the platform, where else are they going to get it? The only other tool they can afford is Microsoft Project, and all that integrates with is Microsoft Excel, and that's not a Procurement tool. Moreover, project management and the workflow it enables is what not only enables closed-loop procurement but seamlessly ties in the one-stop shop and budget management where and when it is needed.

## **Summary**

Proper Procurement is critical to SMB success as it is the difference between identifying savings in a sourcing project and actually realizing those savings. However, this success is still out of reach of the majority of SMB Procurement organizations as they don't have an end-to-end Procurement platform that supports the Procurement process that they need to succeed.

For a SMB, this process relies on a platform that provides a one-stop shop to find the goods and services the organization needs, a closed-loop process that ensures that everything is done properly from requisition to payment, budget integration to make sure all spending is on budget, and project management to make sure that all of the needs associated with the project the purchase is for are met. Anything less just won't do.

## About Sourcing Innovation

Sourcing Innovation, which started in June of 2006, is a leading resource for sourcing, procurement, and supply management professionals who are interested in improving themselves and the overall performance of their supply management organizations. Sourcing Innovation is education about, and in-depth analysis of, technologies and approaches that can have a profound impact on the way an organization conducts business. More information about Sourcing Innovation can be found on the blog itself, at <http://blog.sourcinginnovation.com/>.

