

PROCUREMENT OUTSOURCING: The 10 Things Companies Really Want to Know

By Jason Gilroy
Vice President of Outsourcing
ICG Commerce

As featured in:



Over the past year, ICG Commerce has seen an unprecedented level of interest in procurement process outsourcing. Many industry thought-leaders have launched comprehensive studies on the topic, reporting that performance has exceeded early adopter's expectations and are projecting 15 to 50% growth over the next three years. Trade media and educational organizations that have historically avoided the topic are now approaching it proactively, including The Institute of Supply Management who recently included Procurement Outsourcing on their 89th annual meeting agenda. But perhaps the most direct evidence of a growing trend toward procurement outsourcing from ICG Commerce's vantage point is the 10X increase in the number of inquiries and RFPs we have received for outsourcing services.

While this increased interest in procurement outsourcing is clear and the value proposition can be compelling, many companies still seem to struggle to understand procurement outsourcing and determine the appropriate path forward for their own organization. Drawing upon recent discussions with dozens of companies that are exploring outsourcing services, my colleagues and I have compiled a list of common *questions, behind the questions* and have attempted to provide practical, real-world answers based upon our experience delivering procurement outsourcing services to over a dozen companies throughout the past four years.

1. What exactly *IS* procurement outsourcing and what is being outsourced?

This is perhaps the most basic question but it is a difficult one to answer. What one company views as procurement outsourcing, another may view as a consulting or technology service. In our view, genuine outsourcing differs from other procurement services based on the level and degree of on-going accountability placed upon the services provider. Procurement outsourcing typically involves long-term (36 – 60 months) day-to-day management of a group of procurement sub-processes (e.g., requisitioning, supplier management) for multiple category groups (e.g., Administrative Supplies and Equipment, Industrial Supplies and Equipment, Telecom, IT Hardware, Travel, etc).

Services provided on a consultative or an outsourcing basis each deliver significant value. The more important question to ask is, “ which is more appropriate for my organization?” To determine whether consulting services or outsourcing services are most appropriate, companies should ask themselves (A) is this an area that my company views as a strategic differentiator and are we willing to make the necessary internal investments to become and remain world-class? or (B) is it

an area that, if managed and executed properly, can drive significant value to my organization but does not or will not receive the appropriate internal investment and focus? If you answered yes to (A) then either consultants or a supplemental procurement outsourcing relationship with appropriate knowledge transfer and an exit strategy can help you become world-class. If you answered yes to (B), then full spend management outsourcing can help you transform and become world-class without having to make additional investments in your internal infrastructure.

Most companies we speak to that are looking for a procurement outsourcing partner to assume responsibility for day-to-day management of certain procurement sub-processes are searching for one or more of the following services for a specific scope of categories:

Strategic Sourcing and Category Management

- This typically involves the ongoing strategic management of specific category groups – from understanding expenditures, to developing the most effective category strategy, to driving the lowest total cost of ownership through ongoing compliance, cost and supplier performance improvements. The outsourcing of Strategic Sourcing & Category Management can be a very cost effective way to drive results in categories that either go unmanaged or where the company has very strong procurement resources that can/should be redeployed to more strategic categories or functions within the organization (i.e. direct materials).

Key value proposition: Drive unit cost savings and continuous improvements for cyclical categories that have limited internal resources and expertise

CASE IN POINT:

\$3B bearing manufacturer drives continuous improvements by outsourcing category management

To meet global expansion targets, a major industrial manufacturer established a three-year, \$15 million cost reduction plan. The company teamed up with ICG Commerce to focus on improving the entire procurement process – from sourcing to supplier payment. By identifying savings opportunities in a number of the company's buying categories and by aggregating its total buying volume, ICG Commerce was able to generate significant cost reductions, as high as 36% for certain categories, during the sourcing phase of the procurement initiative. Using a team of dedicated ICG Commerce category managers, the manufacturer is able to continually monitor expenditures and supplier performance across all parts of its organization and, in the process, identify additional ways to further reduce costs.

Transactional Buying Support

Transactional Buying Support services are focused on supporting the day-to-day buying activity that is typically managed by a centralized procurement organization or directly at the end-user level (i.e., plant, site, store, etc). In such cases a provider often uses the customer's existing systems to manage orders and match POs to invoices. Specific activities include:

- Receiving/reviewing orders for accuracy and completeness
- Performing policy validation and judgment for all non-catalog orders, focusing specifically on:
 - Validating requestor's supplier choice, provide requisitioners with "preferred" supplier alternatives (in the event their requirement can be satisfied by a preferred supplier)
 - Enforce customer corporate procurement policy at the point of order, including competitive bid limit guidelines (e.g., three bids required above \$50K)
 - Validate commodity/account codes on non-catalog orders
 - Ensuring accurate pricing for preferred suppliers
- Coordinate the vendor review and add process across the various stakeholders
- Support requestor queries on order status, order exceptions, change orders, etc. for non-catalog orders

Key value proposition: Improve end-user service levels, reduce headcount, improve compliance and reduce process costs

Transaction Automation and Processing

The technology used to help companies automate and streamline their procurement processes can be delivered on a fully managed/outsourced basis. Transaction

CASE IN POINT:

Global energy products and services company improves procurement processes and sourcing capabilities through outsourcing

The company looked to outsource its buying activities as a way to drive cost reductions as well as process and organizational efficiencies. Located at an ICG Commerce facility, resources were cross-trained across commodities to increase knowledge sharing and flexibility to support increasing or decreasing order volumes, which enabled ICG Commerce to reduce the required buying resources by 50% within the first two months of the engagement. Based on projected volume, the company's buying center costs were reduced 40% through the use of ICG Commerce resources.

Automation services include implementation of eProcurement, integration to companies existing ERP or eProcurement systems, on-going catalog development and maintenance, supplier connectivity, buyer and supplier training, spend reporting, and user and system maintenance.

- Ensuring accurate pricing for networked suppliers
- Provide portal to access and determine order status
- Support user questions/queries related to the functional aspects of any buying application as well as Level 1 technical questions.
- Support invoice matching and exception reporting by comparing the supplier invoice with the originating PO.

Key value proposition: Improved spend visibility, compliance and process efficiencies without large investments in software and on-going maintenance.

2. Does procurement outsourcing mean I have to lay-off half of my department and transfer activities off-shore?

No. Procurement outsourcing offers companies the ability focus on their core competencies and gain access to leading external capabilities in non-core activities, ultimately improving the overall level of procurement performance and results across *all* categories and activities without making large infrastructure investments. We see many companies looking to outsource what they either cannot manage well with their given resources and technology (thus reallocating to more core activities) or cannot manage at all.

We've also found that to be most effective in supporting the organization, a procurement function needs to be tightly connected to the organization as well as the supply market. Even in today's global economy, supply markets are still very regional for indirect materials requiring a local or regional procurement presence. Developing a strong end-user to provider relationship is a critical success factor for procurement outsourcing. The most successful outsourcing relationships provide users with easy access to individuals who work in the supplier's market on a daily basis, can speak the end-user and supplier languages, and are knowledgeable about the category, supplier and products or services being sourced.

3. Why do most companies consider outsourcing?

The reasons companies consider outsourcing and the reasons they ultimately decide to outsource are often very different. Many companies investigate outsourcing as a way to lower procurement related labor costs. However, once they better understand the capabilities that Procurement Services Providers bring and how they can use these capabilities to compliment their organization, their decisions are often driven by three key objectives:

- To improve overall procurement performance (i.e. achieve a greater level of cost savings on purchased goods and services) by accessing best in class tools and resources without making additional internal fixed investments
- To gain more freedom and flexibility to focus on core competencies and to apply limited resources to mission-critical business functions
- To attain greater control and reporting on compliance to vendor contracts, SLA's and pricing in addition to their internal procurement policies and procedures.

4. How do I know if procurement outsourcing is the right solution for our organization?

Organizational soul-searching is definitely required. First companies must be willing to outsource procurement and then the internal procurement department has to be able to transform itself from a procurer of goods and services to an effective manager of outsourcing services.

Once you have established your organization's willingness and capabilities, you must define and assess how the business function is performing today, define internal policies and processes, determine desired benefits of outsourcing and decide upon the acceptable level of risk. Too many companies dive into outsourcing without truly knowing what drives their internal costs or how the organization is performing. Without this level of internal understanding, it is very difficult for managers to assess the value that outsourcing can provide. This exercise can be performed internally or with the help of a Procurement Service Provider.

5. Where do I start?

We always tell people to start by gathering the "current state" data first and then move to the more strategic considerations. Regardless of where the outsourcing investigation takes you, a better understanding your current state (e.g., procurement organization throughput, capacity and capabilities) can be a valuable input to any improvement

initiative. Gathering this information ahead of time greatly accelerates the “design” phase of the outsourcing relationship.

Current State Information:

- Spend: by category by location
- Transaction volumes by type: catalog, non-catalog, PO, P-card, spot buy, etc.
- Clearly defined process, organization and technology landscape
- Procurement roles, major activities and percent of time on each

Strategic Scope Questions:

- What procurement activities are market differentiating?
- How will responsibilities be split between customer and provider?
- What is the scope – categories, locations, etc?

Moving on to scope. Selecting the right scope requires careful consideration and a delicate balance. Companies, of course, want to drive maximum value from their procurement outsourcing relationships. Maximizing the value from the procurement outsourcing relationship requires that the relationship have a broad category and process scope. Given this, companies must strike a balance between the desired value from the relationship and the company’s experience and willingness to enter into a broad outsourcing relationship.

Companies typically define the scope of their outsourcing relationship based on a set of categories and processes. A key factor to consider is that the greater the process scope a Procurement Services Provider has over the categories being managed, the greater ability the provider has to leverage its market knowledge and customer experience to drive value. In our experience, small pilot programs very rarely work due to the amount of commitment, effort and level of results needed to show success. The most successful outsourcing relationships strike a balance that optimizes the service provider’s key strengths and a company’s strategic goals and capabilities.

CASE IN POINT:

Growing IT service provider outsources subcontractor labor procurement to ICG Commerce

Looking to find new efficiencies and increase the effectiveness in the buying of contract labor services – the company’s largest and most strategic external purchase – a fast-growing IT service provider partnered with ICG Commerce to manage all aspects of subcontract labor procurement on the company’s behalf. The ICG Commerce team provides the entire range of purchasing expertise, resources and technology necessary to strategically automate and manage all aspects of the engagement. The team managers have complete visibility into request status, real-time labor tracking, invoicing and payment. Preliminary results of the multi-year initiative have reduced the company’s contract costs 10-12 percent.

6. What should I look for from a partner?

Well... of course we are biased when it comes to Procurement Services Providers, but our bias comes from what we've learned providing procurement outsourcing services to over a dozen companies and what it takes to create value in an outsourcing relationship.

Companies should look for providers that have true operational experience in procurement management. Providers that only bring general BPO, consulting, or technology solutions to bear generally do not possess the know-how or ability to effectively take-on and manage both the strategic and day-to-day activities of a procurement operation. These providers often lack the critical mass of experts, process support and technology to deliver maximum value. Procurement can be a strategic and high impact function and requires a tailored solution and experienced partner. Specifically we recommend companies look for experience, leveragable infrastructure and focus.

Experience – Providers should have long-term relationships (over three years) providing comprehensive spend management services (sourcing, transactional buying and processing support, hosted technology and on-going category management) for more than just a handful of companies. The provider should have a track record of success across industries, a solid balance sheet and growth plan, plus a proven commitment to procurement outsourcing.

Infrastructure – To improve performance companies need much more than a cadre of cheaper resources to take over procurement activities. Providers should bring sourcing and category experts, best practices, and flexible technology and tools to automate and streamline processes which they use to drive continuous improvements.

Focus – We are often asked our strategy and I'm always pleased to say that it has not changed over the last four years and won't for the foreseeable future. We do all of procurement and procurement is all we do. If you are outsourcing to focus on your core competencies, wouldn't you outsource to a provider that views that function as it's core competency?

7. How should I gauge a provider's capabilities?

This one is simple: look for tangible examples of a providers operational capabilities, commitment to performance improvement and their ability to "get the work done".

Examples include:

- Process specific expertise – sourcing, buying, category management
- True sourcing and category experts with decades of experience with Fortune 100 companies
- A living and breathing purchasing factory – integrated processes and co-located teams processing orders, managing suppliers, and sourcing categories
- And, of course, the names and contact information of at least three current reference customers

8. How do I get my organization prepared?

In this era of concern over the personal or job-related impacts of outsourcing, you cannot over communicate. Many outsourcing arrangements yield positive changes for employees. Make them aware of your intentions, plans, transition approach and timing and the benefits to the function and the organization.

Internally within the procurement function, you need to design your future organization focusing on how roles may change for those responsible for managing the procurement outsourcing relationship. Other functions and business groups need to be involved in developing the vision for the future organization as well.

9. How should I structure the relationship for success?

In our experience we've identified five critical success factors.

Relationship Model/Goals: Defines procurement outsourcing goals and aligns incentives for both provider and customer

- What are the company's objectives in outsourcing procurement?
- How are the provider's goals aligned?

Governance Model: Ensures customer/provider alignment, measures procurement service performance, provides issue escalation mechanism, manages procurement services delivery and ensures services deliver results

- What are the service levels required to support your procurement team and users?
- How will service levels be measured and rewarded?

- What is the relationship management structure between company and provider?
- How are issues tracked, managed and escalated if necessary?
- How often is status reported and to whom?
- What is the process for issue tracking, management, escalation and resolution?

Transition Management: Maximizes procurement benefits while minimizing disruption and risk to the business

- How will the provider learn the customer's business?
- How will the provider know the services to provide by category by location, etc?
- How will the transition occur?
- What is the plan to communicate the new relationship and services to the broader organization?

Flexibility: Ensures as corporate goals might change, the outsourcing relationship can change with them

- How are changes to the service requested, evaluated and implemented?
- How are business changes managed by the provider, e.g., changes in volume or spend?
- What is the impact on services and fees?

Information: Actionable reporting and information required to achieve procurement outsourcing goals

- What information is required to assess if the provider is meeting SLA's and performance goals?
- How will this information be gathered?
- Who will it be reported to and how will it be used?

10. How can I ensure that I am getting the desired results?

It may seem simple, but “what gets measured gets done”. By clearly defining your expected results and the associated metrics, you can go a long way to ensuring that you will achieve those results. No one criterion can define success or failure, but a combination of the metrics below can focus the relationship on the right results.

- Savings Target
- Process Compliance
- Staff Retention
- Customer Survey Results
- Preferred/Approved Supplier Compliance
- Supplier Reduction – Source suppliers vs. Total Suppliers
- Transaction Accuracy
- Catalog Accuracy
- MWBE and Small Business Spend
- Call Center Metrics
- Number of Agreements Implemented
- Invoice Reduction

At ICG Commerce we have been providing procurement outsourcing services for more than a dozen customers for over four years.



Headquarters
2520 Renaissance Boulevard
King of Prussia, PA 19406
tel 877.935.ICGC
fax 877.ICGC.339
www.icgcommerce.com