HOLISTIC SPEND MANAGEMENT
GETTING A GRIP ON YOUR TAIL SPEND

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THE SAFE, accepted way of thinking runs like this: If you split your spend into what’s manageable and what’s not, you can invest resources on ‘addressable spend’. But who ever made a name for themselves with the safe, accepted way of doing things? More importantly, it could be a trap to continue to think of tail spend as something that can be ignored. And while procurement organizations in the early stage of development are probably best advised to target achievable goals and ever-popular low-hanging fruit, can the same narrow focus be afforded to those further up the maturity curve? In these pages you’ll find thought leadership and examples of organizations’ success that demonstrates ways to tackle waste and to better align with finance in these tricky areas. Not having the interest or capabilities to take on these challenges is fast becoming a costly omission.

Steve Hall  
Editor,  
Procurement Leaders

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IN THEORY, the business impact of e-procurement should be hugely positive. It ought, for instance, to be significantly easier for buyers and sellers to locate and transact with each other, leading to improved sourcing and lower prices. Transaction costs should fall. And payment cycles should accelerate and become more efficient, as error-prone paper documents are replaced by automated electronic ones.

But the everyday reality of e-procurement – as many buyers and sellers know to their cost – is rather different.

In many cases, transaction costs have not materially changed, organizations complain. Moreover, the impact on supply bases has been muted, with much sourcing carried out as before. And instead of a seamless electronic procure-to-pay process, many organizations report that their post-invoice approval and payment processing systems...
post-invoice approval and payment processing systems remain sluggish, manually intensive and error prone.

In short, the supposed brave new world of e-procurement – where all of an organization's suppliers transact with it electronically – remains elusive: paper-based ordering, invoicing, and payment continue apace.

Yet look closely, and there is a common link between all these unwelcome developments: the size of an organization’s ‘tail spend’ – in other words, the extensive range of suppliers, spend categories, products, and services that have not yet been embraced by the organization's chosen e-procurement platform.

Because it’s with the suppliers, spend categories, products, and services that lie within this tail spend where the problems are arising, rather than with those suppliers, categories and products that have successfully been transitioned to the organization’s e-procurement platform.

All of which poses an obvious question: why does the tail spend problem occur in the first place? If an organization makes a significant commitment – and financial investment – in e-procurement, why does it find itself with a ‘tail’ at all?

Talk to those close to the issue, and it’s not difficult to see some of the challenges facing businesses.

**Tough nut to crack**

To start with, points out Dr. Carlos Mena, director of the Centre for Strategic Procurement and Supply at Cranfield University School of Management, procurement functions tend to use a Pareto-like ‘80-20’ approach to e-procurement initiatives, working first to target major categories of spend, and major suppliers. The inevitable result: what is left might only be 20% of the spend – but it’s likely to embrace 80% of the suppliers and 80% of the transactions. Hence, of course, the problem.

“By its very nature, the tail is complex,” notes Mena.

“It’s a hard-to-tackle mass of small commodity-type items, services, ‘one-timebuys’, trivial, they add up to something that’s quite significant.”

Nor does the evolutionary nature of many organizations help, adds David James Ward, Head of Procurement for Europe, Canada and emerging markets at international healthcare firm Merck.

“Most organizations have grown organically over time, with business units, sites, and countries opting to source their own products and services for reasons of cost, convenience and choice – resulting in a massive supplier base of small local suppliers,” he says. “And when procurement functions tackle this, they generally go for the low-hanging fruit, which reduces the tail, but doesn’t eliminate it.”

Another challenge: the difficulty of persuading this amorphous mass of low-value suppliers to engage with a business electronically. For significant and high-value suppliers, the commercial imperative naturally
helps to overcome any roadblocks. It helps, too, that large and sophisticated suppliers generally have the appropriate internal resource to handle the switch.

But in the tail – by definition – suppliers are not significant or high value, and they are generally not large or sophisticated either. And from the buying organization’s perspective, as they move into the tail, resource constraints can make it difficult to bring low-value suppliers onboard in a cost-effective way – especially those with whom the trading relationship is sporadic and infrequent.

Typically, for instance, a procurement function will find itself not only needing to persuade suppliers to sign up, but also being required to send them log-on credentials, user manuals, and to provide a ‘help desk’ capability. Worse, suppliers can and do actively resist not only the implicit costs of an electronic relationship, but also the explicit costs of electronic relationships in the shape of listing fees, platform fees and transaction fees.

“Supplier onboarding is an extraordinarily difficult problem,” notes David Dobrin, President of Boston, Massachusetts, analyst firm B2B Analysts. “Companies were looking for solutions ten years ago, and are still looking now. It’s expensive for the buyer, and expensive for the supplier—especially when they have to pay a fee to join a marketplace simply in order to send an electronic invoice to a customer that they trade with maybe twice a year.

Experts often warn that supplier fees can put businesses in a position of charging significant sums of money to their most important suppliers simply for the privilege of sending an invoice.

And as if these difficulties were not enough, the challenges of onboarding services spend add significantly to the problem of eliminating tail spend, observes Tripp Shannon, Chief Operations Officer at Perfect, a global e-procurement and business network provider.

“For services, the process of procurement is much more complex than with the standard repeat procurement of catalog items,” he says. “Quite often, the cost of a given service requires isn’t known beforehand, and the supplier to notify the buyer of the amount payable at the point of invoicing, which isn't the usual procurement process.

And when the invoice is
Tail spend is a problem, but one which some organizations regard as just an annoyance and an irritation. But you are arguing that it’s more strategic than that. Why?

Two reasons. First, tail spend is the least managed area of spend, and so it’s the area where you’re most likely to find waste. And it’s also the area where you’re most likely to find errors, which add to processing cost. So a lot of the problems are in the tail spend area. But so too are a lot of the frictions between finance and procurement – prices on invoices and purchase orders not matching, invoices coming in without PO numbers, and so on.

In summary, the tail is a lot more trouble to the organization than the level of spend would indicate. It’s disproportionate.

So why do supplier onboarding initiatives fail to tackle the problem?

There’s no single reason. But there’s no doubt that resource
Similarly, organizations help themselves by putting in place processes to constrain the need to generate small low-value transactions in the first place, new products, changes to existing products and so on,” he points out. “Typically, all the effort goes into bringing these new products on-stream, and not enough effort goes into closing down the tail of old and superseded products. So companies carry on manufacturing small runs of semi-obsolete products that they should not be producing. It’s not enough to say: ‘Customers appreciate the range that we offer.’ There needs to be some joined-up thinking about product deletion and rationalization.”

Meanwhile, Merck’s Ward advocates data cleansing and supplier rationalization as a way of distinguishing between the potential tail of spend that an organization might have, and the real, irreducible tail if no further steps are taken. “Typically, there will be suppliers who’ve been used a handful of times, and are unlikely to be used again, but who still sit on the database,” he points out. “Before going into any tail spend initiative, there’s a significant upfront exercise in cleansing the database and seeing exactly what you’re dealing with.”

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notes Hugh Williams, Managing Director of Supply Chain Consultants Hughenden Consulting. “When you look at what creates the actual demand for the items being bought as part of tail spend, a lot of it can be down to things happening at the other end of the supply chain; constraints play a part – which is why we offer an onboarding service – and also no doubt that the underlying vendor master records also play a part, even when suppliers are otherwise willing to sign up. Typically, data goes back over multiple enterprise resource planning (ERP) systems, and it just isn’t clean enough. And it’s always hard to justify the return on investment of a data cleansing project. Our view is that holding supplier data in the network is the right place for it: the supplier has a vested interest in inputting it, and in keeping it current. Plus, they enter and update it just once, for all their customers on the network.

You’re not the only e-procurement provider out there, of course. How would you say that Perfect differs from other major providers? It’s about the business network, and the added value that we provide by processing information passing between buyers and sellers. So as a result, we permit a much richer exchange of documents and information between trading partners. It’s the difference in the richness of a conversation with a 2,000-word vs a 200-word vocabulary”.

And this takes place in the cloud? Absolutely. We say: process information in the cloud, because that’s where it makes sense to process it. Why has a supplier gone to the trouble of submitting an invoice, which you then process behind the firewall on your ERP system, only to then reject for some mismatch, when instead you can process against the buyer’s matching rules at the point of submission, using information already present within the network, and detect and fix any errors then? It doesn’t make sense. So we like to say that we’re a cloud solution that gives buyers and sellers those things that they’d get from an on-premise application, without the compromises that the cloud sometimes entails. You’ve got all the benefits of a cloud application without compromising integration integrity–because it is right there, on the network.
Defining the goal
Even so, some difficult challenges remain. Whatever the resolve of an organization’s procurement function, resource constraints must be overcome, and ways found to make 100% e-procurement not just an objective, but a practical proposition.

The difficulty: inter-linkages between different pieces of the puzzle. Why go through the hassle of onboarding a services supplier, for instance, if there is no meaningful way to order, invoice, and pay for those services? Likewise, even when a meaningful way of ordering, invoicing, and paying for products and services does exist, supplier onboarding on its own will not deliver seamless end-to-end procure-to-pay connectivity. It’s not the placing of a PO that reduces transaction cost, but the associated – and linked – raising and processing of an electronic invoice.

“Organizations are automating the enterprise, making it efficient and transactional, but without really looking at end-to-end process flows,” says Supply Chain Insights’ Cecere.

“Research that we’ve undertaken shows just 33% of orders getting through the end-to-end procure-to-pay process are ‘hands-free’. In that context, supplier relationship management is an oxymoron, because there’s never really a focus on the relationship.”

Nevertheless, she continues, there are reasons to be optimistic – despite an undeniable fragility in many supply chains, following the capacity retrenchment that took place in the aftermath of the 2008/2009 financial crisis and ensuing recession.
I’m excited, right now, because I’m seeing technology start to make these end-to-end process flows actually work,” she notes. “Business networks are offering a new way to define relationships.”

Network efficiencies
Certainly, Perfect – one such business network – aims to turn upside down some of the conventional logic surrounding buyer-seller trading platforms, a move described by Perfect President and CEO Hamp Wall as “quite deliberate”.

He said: “We don’t just pass documents back and forth, acting as a conduit as documents flow from being behind one firewall, to being behind another.

“We try to take the information passing across our network, and add value by allowing trading partners to carry out collaborative processes together, before the documents disappear behind their respective firewalls.

“Electronic invoicing is great, but the issue isn’t how long it takes to submit an invoice, it’s how long it takes to approve it.

And by taking all the approval rules, and putting them on the network in the cloud, suppliers can check their invoices dynamically against those rules as they submit the invoice.

“They know that there won’t be any queries raised because they’ve met the approval rules from the outset.”

Likewise, he adds, while Perfect offers a supplier onboarding service, the nature of the network is such that far from resisting signing up, suppliers have a positive incentive to join.
“We take the view that not only is it the supplier who has the greatest interest in ensuring that data held about them is correct, but it’s also the supplier who is likely to be the best source of that data,” Wall says.

“Yet the practice of keeping the vendor master record tightly held behind the firewall runs directly counter to that – so we say, instead, hold it in the network, where it’s readily accessible to both parties.

“Better still, that way the supplier specifies their data just once, yet it's accessible by every customer they trade with over the network.”

Even so, on its own, providing suppliers with a commercial and operational incentive to sign up to the network is not enough, insists Perfect’s Shannon it’s also important to make that sign up as painless as possible.

“Being free to join is important; that eliminates issues over cost and concerns around what level of fee is proportionate for occasional transactions,” he points out.

“But it's also important to be easy to join, as well as free to join, with very few clicks required and no need to provide extensive amounts of information.”

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