Beyond Stationary: Industrial Strength P2P

Applying purchase-to-pay best practice to direct spend categories

A Purchasing Insight White Paper by Pete Loughlin

Executive Summary

Let's face it, despite its 20-year heritage, e-Procurement has gone no further into the enterprise than stationery and other indirect categories in most organizations. Automating the complex purchasing processes for direct materials has remained an elusive goal for most organizations, and automation is really only achieved by heavily customizing ERP modules.

Point even a world-class e-Procurement solution at a complex direct purchasing process and it will shrug its shoulders and give up.

Most e-Procurement implementations address the indirect purchasing process — a simple linear process that goes from requisition and approval through PO creation to receipt, match and pay. Despite its simplicity, it is surprising how many organizations struggle to automate even this process.

Compare this with a direct material purchasing process in a manufacturing organization where the complexity is compounded in every possible dimension. POs can be multi-page long with literally hundreds of line items. And these orders don't remain static. An order with many lines may undergo multiple changes prior to delivery. Any single variable within a single line item may change the complexion of the entire order — from pricing to delivery dates and anything in between. Point even a world-class e-Procurement solution at a purchasing process like that and it will shrug its shoulders and give up.

This is where Nipendo is proving its strength. Delivering a best-of-both-worlds solution, it offers the cloud-based simplicity of e-Procurement but can manage the intricacies of even the most complex supply chain situations that traditionally relied on heavily customized ERP modules or tailor-made in-house systems.

e-Procurement: and Great Aspirations

e-Procurement emerged in the 1990s as a means of distributing the workload of buyers. Simply stated, it was a way of empowering requisitioners — end users — to buy things themselves using a controlled process. The theory was that you could relieve professional buyers from the humdrum and routine work of raising purchase orders so that they could concentrate on more value-adding activities. After all, who needs an expert buyer to buy a few pens? And when you add up the cost of the purchasing process, from requisition to approval and then add in the paperwork and the postage, the process itself costs more than the pens themselves. Instead of the traditional paper process, why not provide users with a catalogue on their computer providing details of approved suppliers' products with contract pricing? At the click of a mouse, the pens can be delivered — circumventing the procurement team who are busy frying bigger fish.

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It may seem old hat — obvious even — but in 1995 this was cutting-edge thinking; the future promised by e-Procurement was dramatic. B2B marketplaces that promised to automate supply chain processes caught fire. Solution vendors such as Ariba and Commerce One gained multi-billion dollar valuations, and the ERP providers were forced to take notice. By the turn of the century, e-Procurement had established itself as a best practice. No self-respecting organization would think in any other way than to use online catalogues and workflow-based approvals.

This progress didn't come without challenges. The e-Procurement framework was modeled on the most basic of purchasing processes for indirect spend items such as stationery. This made sense. It was the value of the transaction compared to the cost of the process that made this opportunity compelling, and the process that was being automated was simple: Request a low value, low risk item; Seek approval; Order; Receive; Match; Pay. What could possible go wrong?

As long as the process is applied to simple purchases, not much can go wrong. Naturally, organizations started pushing the boundaries of these solutions. And once they attempt to apply these processes to more complex spend categories — there's a great deal that can go wrong.

e-Procurement: Disillusion

Despite a couple of decades of development and deployment in the real world, e-Procurement has failed to scale beyond its initial realm of indirect spend (and even there with just limited success). When we look at real world examples of how the purchasing process has been automated across many industries, we see e-Procurement focused on simple, indirect spend and ERP modules — usually heavily customized — aimed at core business procurement. The difficult indirect spend falls somewhere between the two ends of this spectrum.

It is not uncommon to see businesses with multiple purchasing system for direct and indirect spend.

It is not uncommon to see businesses with multiple purchasing systems — the lightweight e-Procurement system that creaks under the weight of anything more complex than pens and paper and a heavy weight ERP module that can eat the direct spend for breakfast but requires expert users and would be like a sledge hammer cracking a nut if it were applied to indirect spend. Everything in between is supported by manual or uncontrolled processes, as we can see in the following examples.

IT

This seems straightforward — indeed IT is one of those categories that can be easily catalogued. It is slightly more complex than stationery in that there may be a technical approval step in the workflow but at first sight it should be easy.

So you buy an ERP system using a catalogue? Of course not — that's ludicrous. You could buy other routine IT items like desktop computers. But you still need to think how they are commissioned — how they are put together for the end-user. How do you manage the receiving process if they need to get delivered to the IT team before they are delivered to the users. This is not insurmountable, but also not entirely straightforward. When it comes down to it, standard consumables and peripherals are the only IT item that can be easily bought using e-Procurement.

Legal

This is a category that should be simple. But it's not. How can you e-procure — or even just use a purchase order for legal spend? You don't know how much the lawyers cost until they give you the bill. How do you prepare the PO? Please provide one defense against a lawsuit? At what price? There is no catalogue for legal spend. Each piece of work is unique. It can't be done — not in the way stationery is done at least.

Utilities

There are lots of categories for which it's easier to simply pay an invoice when it's received. You can't know in advance how much your utility bills will be. So just pay them. It can be difficult to put utility spend through a purchase order process, never mind an e-Procurement process.

Direct Spend

Last but not least, direct spend. What is direct and what is indirect depends very much on the business. Each industry has its own "direct" spend. It is perhaps best thought of as spend that relates to core business, and especially goods that are used in assembling the products or services delivered to customers. For example, an auto manufacturer would treat sheet metal or paint as direct spend. There's a world of difference between indirect and direct spend. The risk profiles are different; the relationships between buyer and supplier are different; and the purchasing processes are different. Sheet metal, for example, cannot simply be bought from any supplier. The supplier may need to understand the manufacturing schedule and be able to guarantee delivery timescales. The quality and consistency of material is important — even crucial. Purchase orders for direct materials may run into many lines and multiple pages. The simplistic approach to the purchase order process suitable for indirect categories simply breaks down when you get to hard core purchasing.

To fully understand why e-Procurement has failed to meet the requirements of all but the most simple spend categories, we need to understand the direct procurement process.

The Purchase-to-Pay Process for Direct Spend

What is needed is a holistic approach that delivers the flexibility of a cloud-based e-Procurement solution with the sophistication to accommodate the most complex supply chain scenarios.

The simplistic P2P process goes like this: Requisition, Approval, Order, Receipt, 3-way match, Pay — in that order.

It's tempting to think that this can be applied to any purchasing process (with a few tweaks perhaps) and to any category.

In the real world, the elements of this process are like confetti — you have no idea in advance which will land first. The invoice is often received before goods are receipted, and it's not unheard of for goods to be delivered before a formal purchase order is created.

Take an example of a buying organization that is a component manufacturer in the automotive sector. Their procurement process starts at the design stage. Once a design is completed, a bill of materials (BOM) is developed, describing all the individual components of the product to be manufactured. Once exploded into its component parts, a BOM could be made up of hundreds of parts to be supplied by dozens of suppliers. It is not unusual for these parts to be manufactured to order by the supplier. Some of the POs generated could have a single PO line some could be multiple pages long containing many lines.

So far, so good. We're still simply generating a series of purchase orders but they're complex. This is a world away from logging into a punch-out catalogue where the only complexity is choosing which color pens to order. But it gets even more complex.

In a manufacturing supply chain, demand management is critical. Techniques like "Just-In-Time" help large manufacturers in industries such as automotive optimize their inventory. Sharing information about anticipated demand allows suppliers to deliver exactly what is required to meet that demand and no more. Exceeding the necessary supply increases inventory costs and impacts working capital. To achieve "Just-In-Time" optimization, suppliers needs to be informed of demand and to be able to react to it. In turn, their own suppliers need to react according to anticipated demand. The industrial-strength MRP systems of the 1980s that evolved into the ERP systems of the 1990s were built to deal with these kinds of supply chain complexities.

When you position simple e-Procurement solutions against the backdrop of these complex processes it is easy to see why these solutions struggle to reach much further than indirect spend. To really reach deep into complex organizations, an entirely different approach is required — a holistic approach that delivers the flexibility of a cloud-based e-Procurement solution and the sophistication to accommodate the most complex supply chain scenarios.

How Nipendo Addresses Direct Spend P2P

The Nipendo approach is fundamentally different from the traditional e-Procurement framework. It recognizes that in the real world businesses operate in highly complex environments.

To begin with, Nipendo automates a holistic process from procurement to payment, rather than just individual transactions. The process may start with an RFP, and would always include at the very least a purchase order or contract, delivery notes (with or without Advanced Shipping Notice), and an invoice.
Every exchange of information between a buyer and supplier encapsulates the entire context and history of the process.

This intricate level of metadata allows to define very specific ways of handling each and every buyer-supplier interaction.

This means, for example, that when an invoice is received by accounts payable, Nipendo is already aware of the entire history of the order, including the pricing and terms, whether the goods were received, when, and in what condition.

Based on this contextual understanding, Nipendo can automatically approve the invoice for payment without any manual touch, or hold it and prompt the supplier to correct any discrepancies.

This intricate level of metadata attached to each transaction allows the buyer organization to define very specific ways of handling each and every buyer-supplier interaction according to the type of order, the requisitioning business unit, supplier location, custom contract terms, and many other variables.

Any of these variables can determine how a transaction will be handled, such as what validations, notifications, and alerts may be part of the workflow. These variables can also determine what a supplier may or may not do (e.g. can a supplier accept only certain line items and reject others, make partial deliveries, or modify delivery dates). Based on this information, Nipendo can also distribute transaction posting to multiple ERP systems, and most importantly, ensure that only validated transactions enter any of these systems.

As mentioned, direct material POs are rarely single line documents — they can run into pages and literally hundreds of lines. Nipendo Supplier Cloud is architected to manage transactions at the line item level — not header level. This means that if a supplier receives an order of five lines and one of those lines subsequently changes, they don't necessarily need a whole new PO. It means that they can accept or reject a single line item instead of the whole PO if there is one item that can't be delivered. If there's a mismatch in a complex invoice created by a discrepancy in one line — just that one line may be rejected and not the whole invoice, all subject to business rules created by the buyer organization.

When dealing with critical supply chain deliveries, collaboration with the supplier is essential. Nipendo allows buyers and suppliers to attach specs, certifications, images and notes to any order, eliminating the need for unstructured and un-auditable phone and email communication that can be a source for missed deliveries and finger-pointing if anything goes wrong.

The bottom line is a win-win proposition for both buyers and suppliers.

And since timing is of the essence in “Just-In-Time” operations, the ability for suppliers to submit advance shipping notices (ASN) helps supply chain coordinators stay in sync with production schedules.

The bottom line is a win-win proposition for both buyers and suppliers of direct goods. Suppliers can deliver more efficiently and more cost-effectively because they know exactly what buyers expect. In return, they get paid on-time more often and have access to early payment options.

Buyers have greater transparency to delivery schedules and confidence they can meet their own production timelines. And since they can approve invoices quicker, they also have more opportunities to capture early payment discounts.

Yet all of these benefits can only be realized with a Procure-to-Pay solution that is capable of modeling buyer and supplier processes in complex purchasing scenarios, way more complex than those that can be addressed by e-Procurement solutions designed for simple indirect processes.

Getting Your Suppliers to Play Along

No matter how great of a system you put in place, getting your suppliers to actually use the system is still a challenge — with many companies never reaching more than 10-20% supplier participation.

So how do you get your suppliers excited about your P2P program?

1. Rapid onboarding / zero maintenance

The last thing suppliers want to do is spend a lot of time and money connecting to your systems. A cloud-based solution with multiple options for quick and easy onboarding and zero ongoing maintenance is the number one pre-requisite for broad supplier participation.

2. Removing complexity

Direct spend processes can be complex, but a good supplier collaboration solution will abstract these complexities and make it easy for suppliers to work with your system.

3. Access to bids

Issuing RFQ's through your online solution gives participating suppliers a leg up on the competition with real-time access to new business opportunities.

4. Streamlined order and change order management

Direct material orders can be extremely complex, and change orders can be a pain for suppliers. Getting change orders online and in real-time makes it easier for suppliers to manage these orders and respond to changes.

5. On-time payments

On-time payments are a great incentive for your suppliers, but you need to make it tangible. Backed by Nipendo's guarantee, you can promise suppliers that utilize the solution on-time payment for 90% of their invoices.

6. Early payments

Suppliers that utilize the solution have access to early payment programs — either through dynamic discounts or third party supply chain financing options.

For more information

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