



## Six Building Blocks to Bolster Procurement Capability

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# Introduction

For a long time, CIPS has identified THREE levers for building procurement capability – PEOPLE, PROCESS and TECHNOLOGY.

CIPS is best known for its myriad of people development options, many leading to its international hallmark of professional competence in procurement, MCIPS. Increasingly CIPS organisational Certification of policies, procedures and processes is recognised as a standard in its own right – MCIPS for the organisation if you like.

And, whilst CIPS understands and researches technology issues in procurement, the hands-on technological support comes from the major software houses in the space such as inter alia SAP/Ariba, Oracle, IBM and Microsoft, as well as a plethora of niche software suppliers along the P2P supply chain.


The growth in ‘technological needs’ is testament to the growing complexity we are forced to manage. Stakeholders are loading procurement with more and more responsibilities and goals to achieve from the supply side, as more and more organisations recognise the opportunities on the supply side and seek the benefits of good proactive supply side management.

Since the GFC, particularly, organisations appreciate much more the risks emanating from the supply side, and want to manage them proactively. Our profession is facing real challenges in managing more and more complex supply solutions to bring the benefits stakeholders (including consumers) increasingly demand from the supply side of business.

So our profession is growing and developing quickly – it is the fastest growing profession in business. Three levers are maybe not enough in future to drive the organisational capability demanded from broadening requirements and busy procurement teams managing enormous spend, risk and complexity to deliver on testing goals. Procurement leaders at the vanguard of the profession may need more than THREE tools in future.

Of course, CIPSA has been continually harvesting thoughts, ideas, research, strategies and case studies on this theme throughout all our channels for some time; and this is evident in all our activities including publications, regional branch events, CIPSA Conferences and training work. The many procurement ‘transformation’ projects beginning, underway and ending in procurement departments around the region have been a rich vein of data and learning to inform our thinking. Common themes have emerged, and this new CIPSA white-paper written by Peter Morichovitis FCIPS captures the essence of many of them.

Peter has drawn on much of his experience leading the procurement effort to enable the construction of the enormous Olympic Dam mining project for BHP Billiton in South Australia, and subsequently as CPO at one of Australia’s largest borough councils Gold Coast City Council in Queensland. He brings a rare twin perspective from both private and public sectors; and the principles seem common.



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Peter identifies and describes SIX key building blocks for improving procurement capability within an organisation: STRATEGY, GOVERNANCE, ORGANISATIONAL INTERFACE, PEOPLE, PROCESS and TECHNOLOGY. His style is usefully brief and drafted in a minimalist note format – it is almost a checklist of things to consider in building procurement capability from the inside out. He offers a working summary of key factors in driving up procurement capability. Peter also makes the point that regardless of the maturity of any procurement team, these SIX blocks have some role to play in building procurement capability within any organisation; although the mix will vary depending on the start point of any transformation, and its goals, which should naturally vary by organisational need.

I am sure this white-paper will offer a useful checklist for busy procurement leaders in driving forward the capability and influence of our profession to build better outcomes for all stakeholders.

Good luck.

**Jonathan Dutton FCIPS**  
Managing Director  
**CIPS Australasia**

Melbourne, August 2012

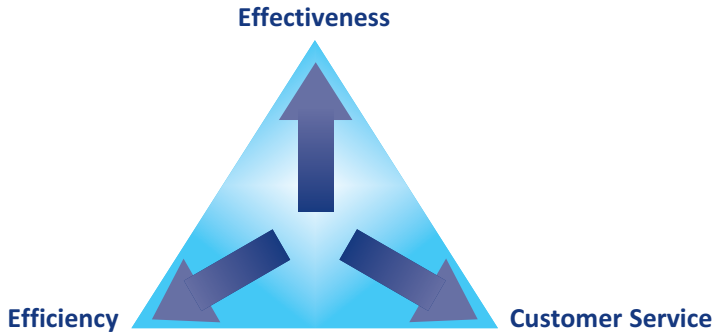
# Procurement Maturity

Corporations can differ greatly in their procurement maturity. Some organisations may be starting out on a journey to improve their procurement function, whilst others may have been on the journey for numerous years, having reached a greater level of procurement maturity and performance and still others are in 'transformation'.

Regardless of an organisation's procurement function maturity, there are six key building blocks to bolster procurement capability within an organisation. If an organisation structures its procurement improvement efforts around these six blocks, it can develop and execute a simple and practical design to improve procurement capability and enable procurement value within the organisation.

## Procurement Value

At the macro level, there are three procurement value propositions or drivers. Corporations may define and measure other procurement value drivers, however, they will, at some level fall within the following three procurement value propositions.



1. **Effectiveness** - reducing the total cost of ownership of external spend using procurement techniques (such as category management, strategic sourcing and supplier relationship management).
2. **Efficiency** - reducing costs from within the procurement function and procurement processes (for example, through process reengineering, deploying technology and automation).
3. **Customer service** - providing best value materials and services to internal customers on time, to specification, above expectation and with social responsibility.

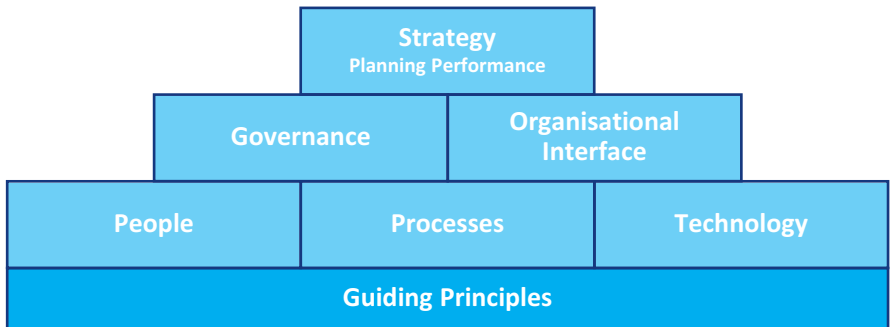
These procurement value propositions often compete with each other, and in some cases are diametrically opposed in nature. As a result, they need to be carefully managed and balanced to optimise value for the organisation.

The six building blocks to bolster procurement capability focus on extracting and balancing effectiveness, efficiency and customer service procurement value for an organisation.

# Six Building Blocks to Bolster Procurement Capability

There are six key building blocks to bolster procurement capability and enabling procurement value within an organisation.

1. Strategy
2. Governance
3. Organisational Interface
4. People
5. Processes
6. Technology



Primarily, from the 'top down', the right procurement **strategy**, associated plans and performance measurement methods need to be built to drive the procurement function. The second row of blocks enables a direct link to the wider organisation through a procurement **governance** framework and the management of the **organisational interface**, particularly with internal customers, executives and suppliers. All upon a foundational layer of **people**, **processes**, and **technology**, built upon the organisation's core values and guiding principles.

# 1. Strategy

*“All men can see these tactics whereby I conquer, but what none can see is the strategy out of which victory is evolved.”* Sun Tzu

It is amazing how many corporations today still do not perform strategic planning activities to drive their procurement function. When it comes to developing procurement strategy, there should be no mystery about it as the process is fundamentally no different to developing other corporate, operational or business unit strategies.

Procurement strategy is concerned with identifying, selecting and implementing the right procurement structures, systems, skills, processes, programs, shared values, initiatives and objectives for an organisation that add significantly to its goals and profitability. In essence, procurement strategy encompasses driving the other five building blocks for procurement capability - governance, the organisational interface, people, processes and technology.

When procurement strategies have been analysed and selected, often the hardest part is the translation of these strategies into organisational action. That's where a linked business planning and performance measurement process needs to be assembled as part of the “strategy” building block.

The following characteristics are commonly associated with successfully laying the “strategy” building block in order to bolster procurement capability.

## Strategy setting:

- A comprehensive long-term (five-year) strategy setting process is operative for developing procurement strategies.
- A clear vision and mission for the procurement function are defined and marketed throughout the organisation.
- The values and guiding principles by which procurement will operate are also defined and marketed.
- The vision, mission, values and guiding principles are aligned with the organisation's strategic objectives, goals and values, with the link actively marketed.
- Procurement strategies and measurable goals to accomplish the vision and mission are defined and applied.
- Risk and total cost are balanced in strategy setting.

## Business planning:

- A comprehensive business planning (annual) process is operative for the translation of procurement strategies into organisational action.
- The business plan details and communicates the procurement strategies, activities, actions, and goals.
- The business plan is the focus of all procurement activity.



## Performance measurement:

- Procurement performance is managed via a balanced scorecard which details the performance measures and goals and is linked to the procurement strategies and business plans.
- Performance measures and goals are aligned with the organisation's strategic objectives, goals and values, with the link actively marketed
- Internal customer satisfaction and supplier feedback mechanisms are incorporated into the performance measures.
- Procurement work group and individual job goals are directly linked to the business plan and balanced scorecard outcomes.
- Performance results are used to review, change and develop new strategies and goals, and continuously improve the procurement function.

## What's the right procurement strategy?

*So what are the right or best procurement strategies?* This is the million dollar (in savings) question.

Fundamentally, there is no 'one-size-fits-all' solution. The right procurement strategy for an organisation is dependent on that organisation's strategic objectives, goals and values, coupled with the maturity level of its procurement function.

The following are essential principles for any corporation's procurement strategy today:

- Risk and total cost are balanced.
- Individual end-user customer and overall company needs are balanced.
- The strategies directly enable the three procurement value propositions of effectiveness, efficiency and customer service.
- Effectiveness, efficiency and customer service value are balanced.
- External influences, such as market and economic conditions, legislation changes and moral obligations are dealt with (eg. security of supply, talent scarcity, carbon tax, social responsibility and sustainability, etc).
- Procurement personnel are allocated to strategic and tactical roles, with technology and automation utilised to eliminate transactional procurement activities.
- The other five building blocks for procurement capability (governance, the organisational interface, people, processes and technology) are built and continuously improved.
- Simplicity.

And the words of Michael Porter also come to mind: *"The essence of strategy is choosing what not to do"*.

## 2. Governance

Procurement governance encompasses control and direction for an organisation's procurement function via a framework of formal structures, mandates, policies, operating procedures, delegations and other decision-rights. Procurement governance is essential in building procurement capability and ensuring the benefits from strategic procurement activities are maximised corporately, as well as keeping the auditors at a distance.

The following characteristics are commonly associated with successfully laying the "governance" building block in order to bolster procurement capability.

### The governance framework:

- Procurement is responsible for all addressable external spend.
- Procurement policies that are simple, based on a compelling business case, and consistent with the corporate culture are operative.
- A clear, company-wide mandate to comply with procurement policies and business plan activities is operative.
- Effective change management has resulted in the corporate culture supporting the procurement governance framework.
- Corporate systems have appropriate controls embedded which support the procurement governance model throughout the organisation.
- Procurement personnel are empowered to make decisions on behalf of the company in accordance with the policies.
- A formal approval framework specifies the authorisation process for procurement spend.
- Procurement actions are based on ethical principles including probity, fairness, impartiality, accountability and transparency.
- Procurement processes, systems, tools and techniques are documented, referenced and maintained as operating procedures, consistent with the corporate standards.

### Some detail - procurement governance essentials:

- Procurement dealings are only conducted with approved suppliers.
- No goods or services are obtained without a valid purchase order.
- Market engagement processes promote effective competition between potential suppliers.
- Formal contracts are operative for high spend or high risk categories.
- Formal authority levels are in place for procurement spend and system generated to optimise processing.
- Confidential procurement information and/or intellectual property are safeguarded.
- Conflicts of interest are minimised and effectively managed.
- Liabilities are provided for and procurement commitments reported.
- Ethical standards are promoted.

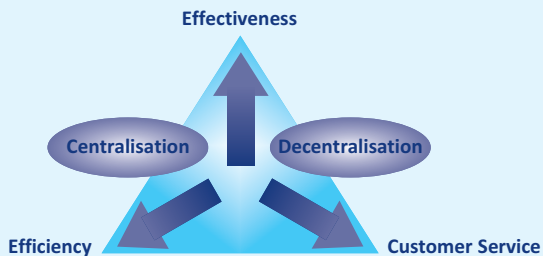
## Centralised or Decentralised?

A procurement governance discussion is not complete without the centralisation versus decentralisation debate. Is a centralised procurement organisational structure more advantageous than a decentralised structure?

The fact that some organisations deploy centralised procurement structures and others favour decentralisation, whilst numerous organisations cycle between the two structures, is a testament to the difficulty of balancing the three procurement value propositions of effectiveness, efficiency and customer service.

Centralised structures naturally (and often unconsciously) tend towards achieving (and prioritising) efficiency and effectiveness value, whilst decentralised structures have a tendency to favour customer service and effectiveness value.

So where organisations believe they are losing efficiency gains, or the corporate culture is not supporting or complying with procurement policies and initiatives (and hence effectiveness value), they may opt for a centralised structure. On the flipside, organisations may feel that customer service (and in turn effectiveness) needs improving, say, as a result of procurement not accurately understanding and supporting customer challenges and priorities, then a decentralised structure may be favoured.



The right procurement organisational structure for a company (similar to the right procurement strategy) is dependent on that organisation's strategic objectives, goals, governance models and values, coupled with the maturity level of its procurement function.

A centralised structure is more favourable for a young, greenfields or immature procurement function, or where a rapid procurement transformation is required. Where the procurement function is of greater maturity and a robust governance model has been institutionalised to the degree that the corporate culture supports the model, then decentralisation is probably the way to go.

The other variable to explore is geographic location. You might have a centralised procurement structure for reporting-line purposes, however, actually co-locating the procurement personnel within their end-user customer areas will assist in providing balance to the three procurement value propositions, particularly around the customer service versus efficiency pay-off.

## 3. The Organisational Interface

*“The greatest ability in business is to get along with others and to influence their actions.”*

John Hancock

To optimise value, procurement professionals need to augment procurement governance with managing the organisational interface. Although governance provides procurement legitimate authority and decision-rights around some organisational elements, a lot of what procurement needs to do to be successful can only be delivered through managing the organisational interface.

Managing the organisational interface is about getting buy-in from key stakeholders regarding procurement strategies, activities and goals. It encompasses leadership, communication, the ability to form relationships, build credibility and influence internal customers and senior executives, as well as get the best out of suppliers. Simply, a procurement professional needs to make or at least influence internal decisions where it has no decision-rights (ie. governance) to do so.

A procurement contract with a supplier may be full of terms and conditions and managed via structured contract performance management activities. Notwithstanding, to maximise the value from the engagement, procurement professionals also need to manage the supplier relationship as a component of managing the organisational interface.

The following characteristics are commonly associated with managing the “organisational interface” in order to bolster procurement capability.

### Internal stakeholders:

- A procurement communication plan is operative and communicates procurement strategies, plans, activities, measures and results.
- Service Level Agreements (SLAs) are in place with customers. The SLAs contain joint strategies, activities, actions, and goals that measure the performance of the collaborative relationship.
- A procurement intranet site, consistent with the corporate standards, is in place to actively communicate and report procurement information.
- A review is undertaken after every ‘project’ procurement performs with/for a customer.
- A customer satisfaction survey is issued to customer groups annually.
- Results from reviews and surveys are analysed, actioned, marketed to stakeholder groups, and used as a driver for the evaluation of procurement strategies and activities.
- Procurement integrates and develops key relationships with internal customers.
- Procurement accurately understands and supports customer challenges and priorities.
- Procurement proactively identifies improvement opportunities in customer areas.

## Suppliers:

- Procurement owns and facilitates relationship development programs with key suppliers.
- Techniques are operative to integrate suppliers into the improvement process.
- Suppliers are included in the organisation's cross-functional teams.
- Joint business plans and projects are in place with suppliers focused on extracting additional value from the collaborative relationship.
- Opportunities and risks are shared with suppliers to optimise procurement results.
- Supplier initiated savings are operative, recognised and rewarded.
- Two-way business information updates are regularly held with suppliers (eg. quarterly briefings, monthly meetings, supplier councils, newsletters, etc).
- A supplier recognition and awards program is in place that formally recognises and rewards supplier contributions.
- Procurement's values, particularly around ethics, safety, environment, community and sustainability are promoted with suppliers.

## What does success look like?

Managing the organisational interface to build procurement capability is arguably the toughest of the six building blocks to accomplish due to its reliance on 'softer' skills such as developing relationships, leadership and influence. So what does successfully managing the organisational interface look like? It might look something like this...

- Procurement has a seat at the table at the highest levels in the organisation.
- Procurement is responsible for all addressable external spend.
- Procurement is an attractive career within the organisation and there is a clear career path within, and beyond, the function.
- Procurement provides a clearly defined professional track for resources striving for executive level positions.
- Procurement has a strategic influence on the conduct of the overall business.
- Procurement strategy is an integral component of the overall corporate strategy.
- The corporate culture complies with procurement policies and initiatives.
- Procurement articulates a credible business case for increased involvement and collaboration in customer areas.
- Procurement is a driver in integrating and developing key relationships between internal customers and suppliers.
- Suppliers are integrated into the improvement process.
- Supplier initiated savings are plentiful.
- Suppliers' share procurement's values, particularly around ethics, safety, environment, community and sustainability.

... in other words, procurement utopia.

## 4. People

The degree to which procurement is able to achieve its mission, strategies and objectives in a corporation is very dependent on the mix and calibre of its personnel and the environment in which it operates. The ability to attract and retain the right mix of people with regard to education, experience, expertise and skills is vital. Consequently, establishing the right environment in terms of roles, tasks performed, motivation, training, career development and reward and recognition becomes critical to the provision of an effective, efficient and customer-focused procurement function.

The following characteristics are commonly associated with successfully laying the “people” building block in order to bolster procurement capability.

### People and performance:

- The best people are recruited, high performers are rewarded and retained aggressively, and underperformers are developed before being managed out.
- Business plan and balanced scorecard outcomes are directly linked to work group and individual job goals.
- The achievement of job goals is in turn linked to performance review systems, incentive systems and remuneration.
- 360 degree feedback systems are in place.
- The work environment reflects the shared values espoused in the procurement business plan
- Personnel demonstrate an overriding commitment to ethics, health, safety, environmental and community responsibility.
- Success is celebrated.
- Well-being and morale are tracked (eg. employee satisfaction, safety, turnover, absenteeism) and actions are operative to increase moral and motivation.

### Training and development:

- Roles have defined technical and personal competency requirements.
- Procurement personnel are assessed against the role competencies and individual training plans are developed and managed to close the gaps.
- People development strategies are regularly reviewed in light of current progress, participant feedback, changes in strategic direction, market conditions and technology.
- Succession planning is operative and linked to training and competency requirements of individuals.
- Training towards MCIPS is actively promoted and facilitated.
- Programs are in place for procurement trainees and graduates.
- Procurement is an attractive career within the organisation and there is a clear career path within, and beyond, the function.

## 5. Processes

Similar to any other corporate function or business activity, processes are a foundational building block for procurement. There is a wide range of procurement processes in the corporate world, however, in keeping things simple (particularly with internal stakeholders), my discussions on procurement processes almost always reference back to the two macro, end-to-end processes:

### i. Source-to-contract

### ii. Procure-to-pay

At a strategic level, the source-to-contract process includes planning for the category procurement exercise, developing the appropriate sourcing strategy, going to market, establishing and managing the contract and supplier relationship; all with organisational engagement and participation.

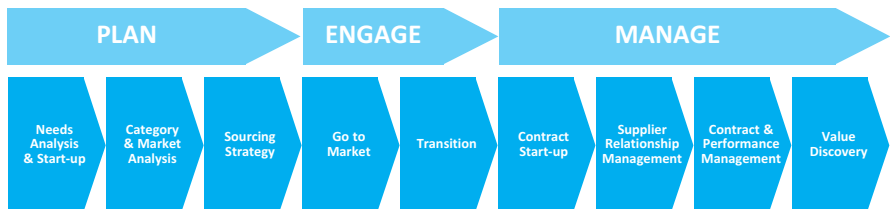
The procure-to-pay process is a transactional process which typically commences with a requisition for the creation of a purchase order and ends with the fulfilment of the goods or services and payment to the supplier. The procure-to-pay process often facilitates purchases from contracts established via the source-to-contract process.

You may know these two processes by different names, or by the numerous sub-process within them.

How does “category management” fit in? CIPS define category management as “the entire art and science of the procurement subject applied to a single genre of expenditure” [ie. category]. In terminology referenced in this document, “the entire art and science of the procurement subject” comprises the source-to-contract and procure-to-pay processes. Or in other words, category management is the source-to-contract and procure-to-pay processes applied to a category.

Briefly, the following seem essential sub-blocks in bolstering procurement capability through “processes”.

### Source-to-Contract:



The plan sub-block plans the entire sourcing initiative and focuses on designing the sourcing strategy for the category.

- Needs analysis and start-up - identifying the need, gathering the baseline data, quantifying the opportunity, identifying stakeholders and initiating the cross-functional team.
- Category and market analysis - analysing category spend patterns, supplier and market conditions, and developing specifications and cost drivers.
- Sourcing strategy - testing and refining sourcing options to create a sourcing strategy.

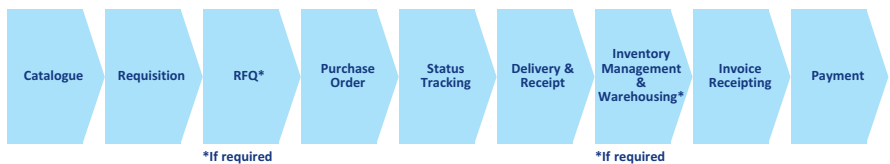
The engage sub-block selects the supplier(s) best able to meet the category objectives, reflects the outcome in a contract, and transitions the arrangement to contract management.

- Go to market - creating the RFx, evaluating proposals and risks, conducting negotiations and selecting the optimal supplier(s).
- Transition - executing the contract, communicating the outcome, developing the operational plan, transitioning to contract management, and conducting a project review.

The manage sub-block implements the contract, and proactively manages the supplier relationship and contract and category performance.

- Contract start-up - implementing the contract.
- Supplier relationship management - sharing opportunities and risks with suppliers to maximise results.
- Contract and performance management - managing supplier and contract performance against category objectives.
- Value discovery - rigorous assessment of category performance and situation as input into the appropriate future category strategy.

## Procure-to-pay:



- Catalogue is searched and drawn upon for the creation of requisitions.
- Requisition is approved.
- RFQ (request for quote) is issued to suppliers and responses are evaluated.
- Purchase order is created and issued to the supplier.
- Purchase order status is updated through expediting sub-processes.
- Physical receipt of the material, validation of hours worked or completion of a service scope or specification is acknowledged.
- Inventory management and warehousing sub-processes for inventory are operative.
- Invoice is matched with the purchase order and receipt.
- Payment is made including the generation of the remittance advice.



## 6. Technology

*“The first rule of any technology used in a business is that automation applied to an efficient operation will magnify the efficiency. The second is that automation applied to an inefficient operation will magnify the inefficiency.”*

Bill Gates

Technology is a great enabler for procurement capability and value. Technology can speed up and simplify routine procurement transactions and lower the cost of information acquisition, analysis and dissemination. Procurement technology ranges from market intelligence tools and e-auctions for strategic sourcing through to an electronic transactional platform for the creation and transmission of procure-to-pay documents.

Integrating an organisation’s source-to-contract process through an end-to-end system and utilising an ERP system to integrate and automate the procure-to-pay process should be high priority for any CPO.

The following characteristics are commonly associated with effectively laying the “technology” building block in order to bolster procurement capability.

### Source-to-Contract:


Technology is operative (preferably in an integrated manner) for the following.

- Capturing, coding, disseminating and analysing category spend information.
- Strategic market and supplier intelligence gathering and analysis.
- Total Cost of Ownership (TCO) modelling.
- Supplier prequalification.
- Creation and distribution of e-RFX and e-Tenders and the subsequent receipt of market responses.
- Reverse auctions.
- RFX and tender evaluation.
- Generating electronic contracts.
- Contract management and supplier relationship management.
- Supplier self-service.
- Reporting on source-to-contract activities.

### Procure-to-Pay:

An integrated (preferably ERP) procure-to-pay system is operative and includes the following.

- Electronic catalogues with consistent coding are searched and drawn upon for the creation of requisitions.
- Requisitioning is online and electronically approved.
- Electronic RFQs are created and transmitted to suppliers; responses are electronically received and evaluated.
- Electronic purchase orders are automatically created and transmitted to suppliers.
- Purchase order acknowledgements and responses are electronically received.
- Purchase order status tracking is e-enabled, including the receipt of electronic advanced shipping notices.

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- Inventory is optimised by the system and automatically replenished.
  - RFID or barcoding technology is used for efficient warehousing.
  - Invoices received from suppliers are electronic (ie. e-invoices) or recipient created tax Recipient Created Tax Invoices (RCTI) are used in-lieu of supplier invoices.
  - Invoices are electronically matched with the purchase order and receipt.
  - EFT is used for payment and remittance advices are electronically transmitted to the supplier.
  - Suppliers view the status of their invoices via the internet or a self-service portal.
  - Purchasing cards and travel cards (eg. Visa, American Express) are used and reconciled electronically.
  - System reporting on procure-to-pay activities is operative.

# Conclusion

In conclusion, it serves to simply reiterate that, regardless of an organisation's procurement function maturity, there are six key building blocks essential for building procurement capability and enabling procurement value within an organisation.

If an organisation structures its procurement improvement efforts around these six blocks, it can develop a simple and practical design to improve procurement capability and enable effectiveness, efficiency and customer service procurement value within the organisation.

## About the Author

Peter Morichovitis FCIPS is a highly accomplished Procurement and Supply Chain leader with diverse experience across the resources, manufacturing and government sectors. He has extensive experience in category management, strategic sourcing and supplier relationship management and over the last 10 years has specialised in leading procurement function transformations. Peter is currently CPO at Gold Coast City Council, Australia's second largest local government. In his prior role Peter was Manager Supply, BHP Billiton for the Olympic Dam asset, Australia's largest underground mine and minerals processing operation and has had a long career in various procurement roles previously with the company. Peter is an accredited Six Sigma Black Belt, and holds post-graduate qualifications in Marketing as well as undergraduate qualifications in Commerce and Journalism.



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Level 8, 520 Collins Street, Melbourne, Victoria 3000, Australia  
**T:** 1300 765 142 (+61 3 9629 6000) **F:** 1300 765 143 (+61 3 9620 5488)  
**E:** [info@cipsa.com.au](mailto:info@cipsa.com.au) **W:** [www.cipsa.com.au](http://www.cipsa.com.au)