



SPEND MATTERS COMPASS SERIES

2010 Volume 2: Spend Visibility and Beyond—Analytics Broader Role in Procurement and Supply Chain

# Analytics and P2P: Using Spending and Payment Insights to Drive Savings and Working Capital Management Strategies



## P2P—Previously a World of Somewhat Nebulous Objectives Grows Up

Harkening back to the early days of the eProcurement market when the likes of Ariba, Commerce One, Intellisys, Rightworks and others pushed their largely vapor-ware on an uneducated procurement buying public, most organizations, then as now, typically latched on to the same basic value propositions for automating their procurement and payment situations. Even though we've come a long way in the past decade in terms of clearing out the vapor, the basic benefits of what vendors now describe as purchase-to-pay (P2P)—and procurement organizations buy hook, line and catalog-requisitioned sinker—haven't changed much. These include, in no particular order:

- Reducing maverick spending activities (i.e., making sure that there are no renegade buys or purchases/payments made to unauthorized suppliers)
- Driving overall organizational compliance
- Lowering overall purchasing costs (e.g., driving spend to targeted suppliers and configuring specifications to avoid unnecessary costs—e.g., extended warranties on technology hardware)
- Implementing procurement controls that stand up to regulatory and shareholder scrutiny
- Ensuring that individuals and departments do not exceed their indirect buying budgets
- Subliminally notifying employees that they're being watched
- Gaining better visibility into spend reporting
- Allowing for enhanced financial forecasting (and rapid control mechanisms, when required)
- Getting rid of paper

### Many companies originally ignored the complexity of P2P, eInvoicing and supplier enablement

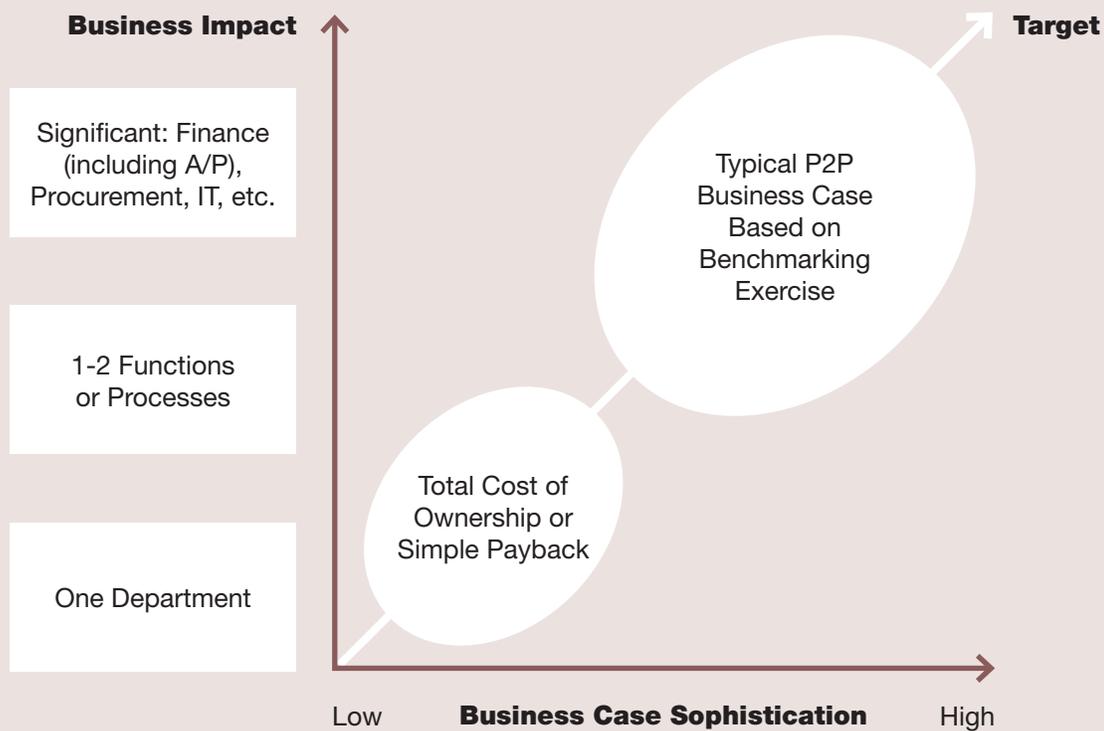
#### OVERLOOKED INITIAL CONSIDERATIONS

- Percentage / share of spend under mgmt. for different categories
  - MRO / catalog
  - Other indirect / catalog
  - Print
  - Services (simple+complex)
  - T&E
  - Direct
- Supplier enablement (initial)
- Supplier enablement (ongoing)
- Content management
- Overall user experience
- Process and technical integration
- Closed-loop compliance
- Invoicing / EIPP opportunity

#### ADDITIONAL COSTS / CHALLENGES

- Cost and effort to manage the accounts payable process (much of it specific to invoice management and workflow)
- The cost of inaccurate information
- Solving the “paper” challenge—that's right, don't think for a minute that P2P or SRM investments alone will get rid of paper
- Realizing there is no “one size fits all suppliers” solution—we must consider the cost of having a lowest common denominator solution
- Regional challenges / barriers and existing operator infrastructure

## P2P business cases based on benchmarking efforts require a greater level of sophistication than most given their overall enterprise Impact



Source: Tech Ventive, Spend Matters analysis

For most companies that have implemented or upgraded a P2P toolset in the past five years, most if not all of these benefits should be a reality today. But while they've become the ante from an expectation standpoint when it comes to P2P results, they do not go far enough in helping companies truly enhance procurement operating effectiveness and efficiency. In today's environment where driving year-over-year cost out of the buying equation with fewer transactional resources is the norm, procurement organizations should take a step back and look at what they could achieve, versus what they are actually (in the majority of cases) realizing today. Spend Matters research suggests that the most powerful approach in defining an ideal future transactional buying and P2P state comes not from what we've expected to achieve in the past, but what we can challenge ourselves to quantify, benchmark, define and measure in the future. Put another way, rather than simply implement P2P (e.g., eProcurement, EIPP, T&E, etc.) systems and related analytical tools to pursue and measure the previously bulleted activities, organizations should first understand both what's possible from a quantitative improvement standpoint and where they are today.

Even up front, this type of exercise is not at all academic—or something that companies should relegate to lower level team members building business cases for investments. Understanding P2P metrics, benchmarks and the organization's current standing can help us answer the following types of questions, all of which are fundamental to procurement strategy and execution:

- What are we really trying to do from a P2P systems implementation perspective—and how should we rank our priorities?
- How important is process and process change as part of an initiative?
- What types of benefits can we expect from reduced labor costs versus other areas?

- Who will take ownership of driving adoption (e.g., making invoice automation the status quo)
- How will our suppliers react to the system and can we expect added—or reduced costs—from new operating models?
- What is our definition of success around compliance and how do we plan to baseline and measure it?
- What is our plan to drive adoption—and to tie upstream and downstream procurement activities together alongside working capital and finance objectives?

## P2P—The Intersection of Benchmarks and Analytics

### **Beyond benchmarks: make sure you've got all the elements of a business case together to maximize P2P change potential**

A complete business case for a high-impact project must include real, tangible financial metrics that address improvements in a company's share price, market valuation, or other wealth-creation driver. But even that's not enough.

#### **THEY ALSO MUST PROVIDE:**

- Realistic benchmarks
- Proof that the new processes, metrics, or software can deliver the expected efficiencies, performance, service, and costs
- Risk adjustments to account for potentially negative business and implementation events
- A data collection and monitoring process for recording the progress and delivery of benefits

Source: Tech Ventive, Spend Matters analysis

Spend Matters research has long considered Hackett Group metrics to be the gold standard of P2P benchmarking. Based on a top-down methodology surveying both finance and procurement executives, Hackett data can help show organizations where they sit on the procurement and payables continuum relative to their peers. As part of the collaboration for the research for this report, Hackett agreed to share with Spend Matters some of the findings from its latest P2P benchmarks. By taking into

consideration Hackett's findings and analyses—and going through such a benchmarking process with Hackett directly—procurement and finance organizations will not only understand where the best places to focus their efforts are, but what the expected impact of new programs will be based on similar outcomes in peer organizations.

Before diving into the details of some of Hackett's recent benchmarks in this area, it is useful to summarize some of the high-level findings that these and related studies show year-in and year-out. In this regard, Spend Matters analysis suggests:

- The gap between top performers, average and lower performers continues to be significant in the P2P area
- The best performing organizations achieve significantly better P2P benchmark results with fewer resources (not just less expensive resources)
- The benefits of P2P automation matter more when it comes to savings and working capital management strategies from an effectiveness perspective than an efficiency one (i.e., labor cost savings rarely outweigh other benefits)
- Fixing broken processes (or addressing a lack of process integration between procurement, finance and A/P) will almost provide a better result than reducing transaction processing costs first through a move to a shared-services or outsourced operating model
- Technology and visibility—not human capital—are the most important strategy enablers (e.g., discounting, payment term optimization) and flexibility
- Cycle time reduction for procurement and order processing not only leads to greater efficiency, but enhanced forecasting visibility and overall procurement and buying controls

- Top performers not only save—they create auditable trails of buying and payment activity that are more likely to stand up to current and future regulatory and shareholder scrutiny

## Order Processing and Invoicing Costs

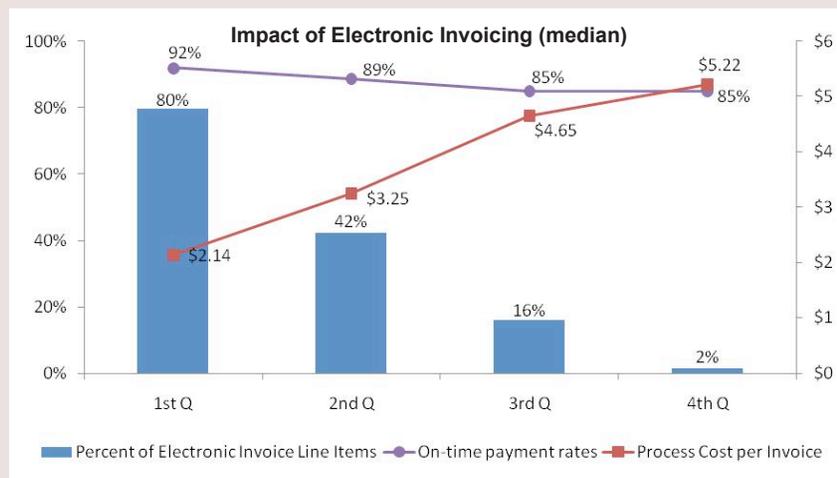
Recent Hackett data suggests that non top-performers spend roughly 60% more in processing costs per order (\$16.71) versus top performers (\$10.04). These numbers factor into account both labor and outsourcing costs. Still, the number for both groups has trended up in the past year, perhaps owing to a notion that Hackett suggests companies are placing a “greater focus on formalizing the purchasing process and driving compliance policy.” This in turn may be contributing to the “rising costs of an order.” In terms of process costs per invoice, non top-performers spend almost 4X the amount (\$3.90) to process a single invoice from a labor and outsourcing cost perspective than top performers (\$1.14).

## Overall P2P Processing Costs

Hackett research suggests there is an 80%+ delta for overall P2P process costs (again, factoring in labor and outsourcing) between top-performing organizations and non top-performers. This differential includes accounts payable labor and related costs as well as purchasing operations costs. Similar Hackett benchmark data takes this analysis further by showing that top performing procurement organizations require less than 50% the level of transactional resources (24) per billion of dollars in spend compared with non top-performers (48.2 FTEs per billion in spend). Hackett suggests that “for the average company benchmarked this equates to about a \$7 million process cost gap between top-performers and non top-performers.”

## Impact of Electronic Invoicing on Early Payment Discounts and Processing Costs

**Learn to use respected benchmark intelligence to your advantage in crafting an overall P2P business case**



Source: Hackett Group

Companies that deploy an invoice automation or electronic invoice presentation payment (EIPP) solution set do not just create process efficiencies—they can also enable greater financial forecasting accuracy and enhanced worked capital management strategies, including early payment discounting programs that can yield over a 20% APR while helping to reduce supply risk. Hackett data suggests that those companies in the top quartile of performance which adopt early payment discounts (and process, on average, 80% of invoices electronically) realize discounting participation rates nearly four times

as high as bottom quartile performers (which process only 2% of invoices electronically). From a cost perspective, Hackett research suggests that true electronic enablement of invoices reduces process costs to approximately \$3.13 per invoice. This compares, on a per invoice basis, with \$4.39 for OCR (optical character recognition), \$5.41 for imaging and workflow and \$7.99 for paper invoicing costs.

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## Truth in Data—Drilling Into P2P Datasets

It's one thing to understand benchmark performance across P2P areas to set strategy, prioritize investments and measure performance, but it's another to unearth the benefits of drilling into P2P-related datasets to uncover savings, audit/recovery and other opportunities. In this section of our analysis, we present some of the possibilities, benefits and outcomes of drilling into different types of P2P data.

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### Stand Alone PO (and A/P) Datasets

Basic yet complete PO datasets can tell us quite a bit under many circumstances. Regardless of whether or not we dump PO information into a data warehouse with a BI front end (e.g., SAP/Oracle), or a traditional spend cube (e.g., Ariba, BravoSolution, Emptoris, etc.), the packaged analytics of our P2P program (provided they're sufficient) or a separate analytics application like BIQ (from where the following examples come), PO data can be very helpful in determining both cost reduction and working capital management strategies.

For example, consider how PO line-level detail including such fields as item description, price, quantity, unit of measure, terms, etc. can tell us such things as trend lines on unit prices (on an apples to apples comparison basis). This type of comparison of actual prices agreed to in a transaction (but not necessarily paid) to negotiated contract terms and overall percentages can yield numerous savings and audit recovery opportunities, as can taking a closer look at PO trending data based on dollar-limits (and what those specific dollar limits may be) compared with those containing item level pricing.

Moreover, PO data becomes that much more useful when we begin to incorporate it with A/P datasets in our analysis as well. Depending on a company's system environment, these combined datasets may or may not come from the same systems. In addition, if an organization has also invested in an invoice automation or EIPP (electronic invoice presentment payment) solution, they may have access to even more granular data in this scenario. The combination of PO and A/P data can help us detect actual prices paid for items as well as anomalies between contracted, PO-approved and price-paid amounts. This can be useful in analyzing spend that is going through PO systems versus that which is not being captured on a granular level (e.g., by vendor, department, individual, geography, commodity code, ERP code or other classification taxonomy).

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### Legal Services

It's possible to achieve material legal cost reductions by looking closely at P2P related information, much of which is often contained within legal billing systems, integrated P2P environments, invoice data and matters management systems. For example, by looking at the combination of these datasets, procurement and legal teams can jointly examine bill

rate compliance, analyze expenses and identify the best mix of in-house, firm and potential offshore opportunities. Traditionally, Spend Matters research suggests legal departments have very limited visibility into their own spending and trending data.

Such analysis activities can help drive overall sourcing strategies (e.g., fixed-price amounts for patent filing and submission vs. hourly billing) based on analyzing overall volume and costs for specific legal / matters activities. They can also lead to better hourly costs from firms based on a clear and transparent understanding of overall activity in specific matters areas, leading to both local and global firm rationalization strategies. Moreover, by taking a data-driven approach to legal spend, both procurement and in-house counsel can come together by agreeing on shared objectives, goals and measurements based on jointly defined and desired outcomes.

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## **T&E/Travel**

Insight into T&E spend, a specialized area that falls within P2P but often outside of traditional eProcurement and invoice automation environments can also yield useful and material results. Analyzing travel agency reservation records, contract pricing, internal organizational hierarchies and internal travel booking system transactions can help organizations identify both immediate and future cost savings opportunities. These savings initiatives might include identification of flights that are out of policy (based on seat or ticket class—e.g., upgradable coach vs. restricted coach) and the rolling-up of missed savings opportunities based on organizational hierarchy (i.e., aggregating losses to show true cost by department and organization).

In addition, P2P analytical efforts that tackle T&E spend can also enable companies to gauge which city pairs (i.e., outgoing / incoming flights), airport care hire and hotel bookings receive the highest traffic (and dollars) to help procurement travel managers focus their negotiation efforts with carriers and by leveraging information as an asset. Such efforts can also help companies identify potential fraudulent activities and transactions (e.g., fraudulent expense submission and reimbursement, phantom vendors, overpayment) and reduce the likelihood of regulatory non-compliance from a lack of financial controls tied to procurement policy and enforcement.

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## **Recommendation: Leveraging P2P Analytics in Your Own Environment**

While P2P benchmarking exercises are most effective when organizations carry them out in a top-down manner—ideally with close finance involvement—P2P analytics focused on category savings opportunities can work from the bottom up. The critical enabling factor in this regard is visibility and cleanliness of data—not to mention an ability to get this information into an analytical environment that allows the flexibility to drill deeply into different types of data sets to unearth opportunities. To simplify the enablement of P2P analytics, Spend Matters recommends that procurement organizations:

- Gain directional indication of where the best opportunities may come from based on initial benchmarking exercises and potentially third-party category analysis
- Invest in a spend visibility toolset that enables the ability to look at both PO and non-PO information
- Develop strategies to integrate non-traditional data sets into a spend analysis environment (e.g., legal, marketing, T&E and related systems data)
- Once you've consolidated the data sets in question in a stable environment, ensure your analytical package is up to the review task (i.e., know the limits of ERP BI, not to mention Excel and Access)
- Find an executive champion (e.g., CFO, general counsel) that will submit their own information for analysis and review, including tax, audit, matters management and related spend data; executive backing such as this for areas of P2P spend that procurement has not been able to previously influence can be critical for building momentum for overall indirect and services spend analysis and sourcing initiatives

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## **Recommendation:** Getting the Most from P2P Benchmarking and Analytics

Spend Matters research suggests that companies which invest in the right sets of technology can drive significantly disproportionate returns when it comes to getting the most out of their overall P2P programs (including both eProcurement and invoice automation) as well as spend analytics. Unlike other areas of procurement (e.g., strategic sourcing) where it's possible to correct for a lack of technology with only a minimal loss of efficiency, provided skilled team members follow processes correctly and employ the right supplier management, supply market and negotiation strategies, P2P is an area where technology can—and should—serve as a core underpinning that drives everything else, from overall purchasing and A/P transformation to advanced sourcing strategy development for categories which procurement was unable to previously impact. Therefore, procurement organizations should look to:

- Create budgets and business plans in this area based on overall business impact rather than just category cost savings or labor efficiency gains
- Leverage the right toolset to radically alter—versus just fix—broken processes
- Put significant effort into evaluating the right set of technologies and associated solutions (e.g., supplier networks) as early in the process as possible
- Leverage third-party services firms not just for systems selection and implementation but for process knowledge transfer
- Try to avoid even considering shared-services or procurement BPO approaches for P2P until the core underlying processes are fixed

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