

## **10 Best Practices for Supply Management Organizations**

**Robert J. Engel, C.P.M.**  
**Senior Practice Leader**  
**Resources Global Professionals - SCM Practice**  
**713-403-1979: [Bob.Engel@Resources-us.com](mailto:Bob.Engel@Resources-us.com)**

**Jon Wesoky**  
**Senior Practice Leader**  
**Resources Global Professionals – SCM Practice**  
**703-610-3423: [Jonathan.Wesoky@Resources-us.com](mailto:Jonathan.Wesoky@Resources-us.com)**

### **95<sup>nd</sup> Annual International Supply Management Conference, April 2010**

**Abstract.** During these unparalleled economic times, leaders of Supply Management organizations are receiving increased focus from their company's C-Suite and Leadership to contain costs and produce results. It is gratifying, as supply management professionals, that most companies are recognizing the importance of their supply chains. This has resulted in supply management leaders taking the necessary steps to move towards implementing philosophies, methods, and processes that will result in their organizations being viewed as Best of Class or Transformational. Supply Management organizational leadership have been challenged with taking the reins to lead their organization to new levels of achievement not only in saving money, but also in improving company performance, effectiveness, and efficiency. This session will focus on 10 specific practices that should be embraced.

**Objective.** To provide thoughtful and meaningful information regarding the key strategies and practices to build a road map for becoming a more effective supply chain organization.

### **10 Best Practices for Supply Management Organizations**

This manuscript does not pretend to have a precise roadmap to follow in order to achieve desired supply chain maturity and excellence. It does, however, offer insight as to the key attributes that should be adopted or addressed. The sequence order of these “10” do not specify or recommend a higher vs. lower importance ranking, but does offer a systematic sequence when developing a scorecard of effectiveness in building a best of class supply chain organization. That said, let's examine these 10 initiatives.

The ten are:

1. Establish a governing council.
2. Align and staff the supply chain organization.
3. Utilize technology and procure to pay.
4. Set the strategic sourcing strategy.
5. Establish key supplier alliances.
6. Manage total cost of ownership.
7. Establish processes and controls.
8. Manage compliance and risk.
9. Optimize company owned inventory

## 10. Establish green initiatives and social responsibility.

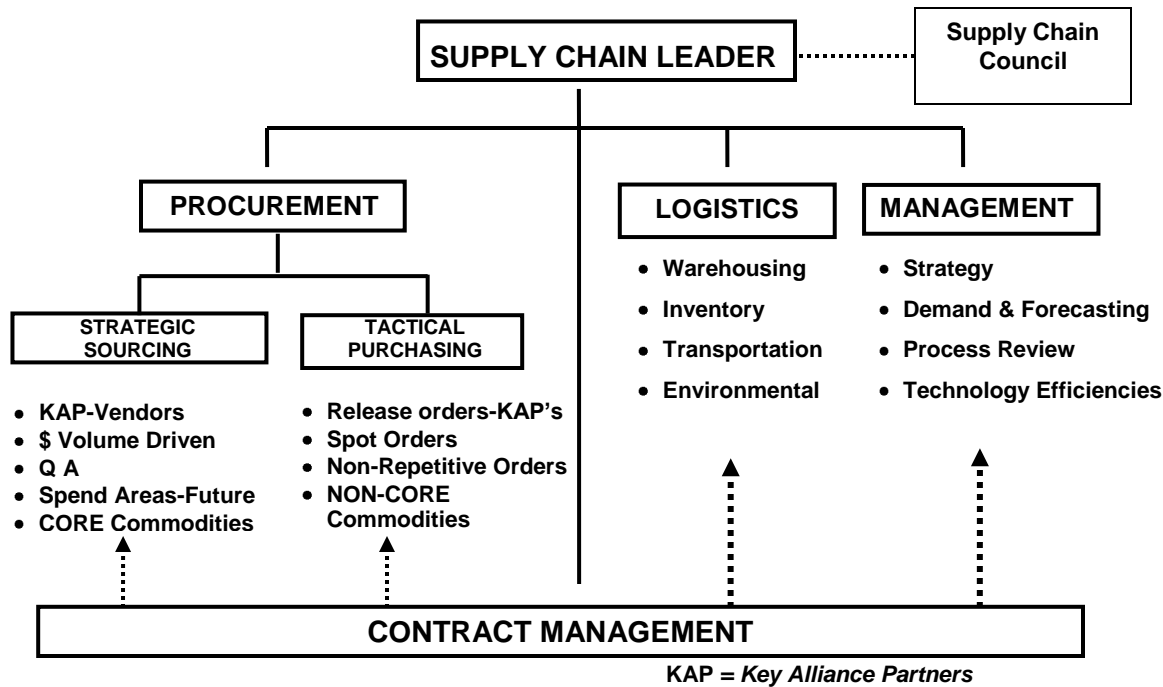
**1. Establish a governing council.** As our first listed best practice, the establishment of a Supply Chain Governing Council is absolutely critical for the success of the company's supply chain effectiveness. Who should be on this council?? Well, certainly the supply chain organization leadership but more importantly it should consist of members of the executive group, key internal business unit leaders, and other influential company leaders. Such a council is so very valuable in that it:

- **Gives direction to and helps align supply chain strategy.** It is very important that the supply chain strategy be in direct correlation with the company strategy. Often we see supply chain organizations that are struggling for recognition because their objectives differ from the stated company objectives. The governing council can provide constant and consistent validation of strategy.
- **Helps in removing barriers within the organization.** Every company has these barriers that are usually those individuals or organizations who don't see or accept the value that supply chain can provide. The operational members of the council can help address, remove, or steer the supply chain efforts in such a manner to ensure that the supply chain organization is given the opportunity to perform.
- **Fosters internal organizational buy-in that is needed to be an effective service organization.** Once the organization sees that the executive leadership is fully embracing the supply chain organization, it is likely the key business unit stakeholders will follow suit and will be more willing to work with and support the supply chain efforts and initiatives.
- **Provides a needed forum for early involvement.** By having an active governing council, the internal business unit leaders can provide the supply management leadership with information regarding future strategies and projects.

**2. Align and staff the supply chain organization.** Once the supply chain council has set a strategy, the supply chain organization must be prepared to execute. One significant challenge has been how to organize the function to realize the full potential and benefit of being an effective organization. Certainly, organizational structures will take on different looks from company to company. For some companies, it is well served to embed a proficient supply management professional in the internal business unit, and for others the most effective way is to provide a more centralized approach. And a "hybrid" approach of these two would also merit consideration. But a leading strategy of progressive companies is in centralizing strategy to gain consensus, with decentralized execution to improve service.

Regardless, the emerging trend in supply management organizational effectiveness is to roll up under the supply chain leader the functions of Sourcing, Materials Management, Logistics, Forecasting/Demand planning, and Contract Management. The following organizational chart is not listed to suggest this chart is correct for all companies, but more so to give a pictorial view of what today's modern organization may look like.

## Supply Chain Management Organization



Correctly staffing the organization is vital to success. As the supply chain function evolves and as we have matured as a vital part of our company's management team, the overall SCM organization skills and knowledge must also be elevated. Leadership is desiring their teams to be more strategically focused, and less concerned about transactional ability. Further, the skill set requirements include:

- Strong interpersonal communication
- Strategic thinking
- Value oriented
- Relationship management skills (both internally and externally)

**3. Technology and purchase to pay.** Best of class supply management organizations are recognizing the importance of technology and an efficient purchase to pay process. The reality is that technology is NOT just a supply chain thing—it is how company's today are conducting their business. ERP systems are being implemented and updated and a general feeling is that we are feeding the system when in reality the system needs to help us become more effective. Best of class companies put in place the strategy and working mechanisms to get the very most out of their technology. As we continue to migrate to a global economy, the need for connectivity has never been greater.

Data is another area that technology can greatly assist the supply management function. Unfortunately, most organizations have difficulty retrieving the type of data (i.e. spend data) needed to make sound strategy and business decisions. Once again, best of class means

finding a way to make technology produce the type of data that is beneficial without having to perform various “work-arounds” to extract and see the required data.

**4. Set the strategic sourcing strategy.** Strategic sourcing is a cornerstone of supply management. A successful **collaborative** strategic sourcing initiative not only ensures availability of supplies, but will result in the obtainment of overall lower total cost, streamlined processes, and increased responsiveness to customers’ changing needs.

Strategic sourcing is not just a purchasing department initiative. It requires input from all functional areas such as finance and accounting, engineering, operations, maintenance, safety/health/ & environmental, quality assurance, and internal business unit team members that will contribute to the initiative’s success. That’s the essence of the collaborative side and the success of achieving true buy-in from our internal clients is getting them involved in the decision making process. After all, aren’t our business units our customers?? And shouldn’t they be actively involved in not only assisting with the decision making process, but more importantly giving key feedback and information regarding their objectives and strategies?

**5. Establish key supplier alliances.** The ultimate success of strategic sourcing depends on the team’s ability to select key suppliers and to manage supplier alliances for critical spend areas. Perhaps one weakness in most strategic sourcing efforts is the follow through with the selected suppliers. In most circles today, this final step has traditionally been called “supplier relationship management.” In reality, perhaps a more appropriate term should be “Alliance Management” since supplier management has a tendency to infer one way communication (telling the supplier how to do it) vs. the correct mindset of two way communication which requires both buyer and seller to team together (Alliance) to manage the relationship.

A primary goal of most supply chain organizations is to channel their relationships with their key suppliers so that maximum focus can be achieved for the major or core spending areas. With a well founded and fundamentally sound Alliance Management program in place, supply management organizations are equipped to use the talents of the supply base to not only create sustained value, but constantly seek continuous improvement. The four primary objectives of an effective Alliance Management program with key suppliers are:

1. Provide a mechanism to ensure that the relationship stays healthy and vibrant,
2. Create a platform for problem resolution, and
3. Develop continuous improvement goals and objectives with the objective of achieving value for both parties.
4. Ensure that performance measurement objectives are achieved

**6. Manage total cost of ownership.** Strategic sourcing shifts the company’s and team’s focus from just looking at the purchase price, to understanding the dynamics of the total cost of owning or consuming a product or service. For significant spend areas, procurement teams are abandoning the outmoded practice of receiving multiple bids and selecting a supplier simply on price. Instead, they consider many other factors that impact the total cost of ownership. In fact, acquisition costs accounts for only 25% to 40% of total cost for most products and services. The balance (and majority) of total cost is comprised of operating costs, training costs, maintenance costs, warehousing costs, environmental costs, quality

costs, transportation costs, and consideration for the salvage value. Identifying total cost requires cooperation and input from both the buyer and seller organizations. It requires: (1) looking at the entire process of procurement and consuming the product or service, and (2) asking our suppliers as well as our internal business units “How can we work together to reduce the total cost of ownership?” Establishing a Total Cost of Ownership mindset is a goal that the supply management organization needs to embrace and perpetuate throughout the entire enterprise.

**7. Establish processes and controls.** In our high tech world, we see an inherent fallacy of companies who first select technologies to make them more efficient and then structuring the processes around the chosen technology. In reality, the focus should be on “what technology is going to help me become more efficient.” The answer will come when you first review the processes under consideration, determining the needs and then select the technology that best satisfies those process needs. Don’t select and install the technology first and then structure the process around the technology. That is a recipe for disaster. Technology should be considered as the tool to help increase efficiency, not the focal point of what is to be done.

And it’s not only the processes and technologies that must be in sync, but we also need to review the supply management policies and procedures as well. Most, as we know, are often found to be culture driven, and do not accurately reflect today’s environment. Review them constantly, and bring them up-to-date keeping them realistic and easy-to-understand and follow.

**8. Manage compliance and risk.** In actuality, supply chain leaders and their teams do negotiate significant potential savings during the sourcing process. However, the reality is that in most cases companies never do fully realize the full extent of these savings. The reasons are varied, but include a lack of communication of contract terms within the organizations and a failure to monitor contract compliance. All too often the fully executed contract is filed away in some drawer and forgotten. Aberdeen did a survey of supply management leaders and raised the following question: “*how do you manage your company’s contracts?*” The answer was startling in that two thirds of the respondents stated that “*we can’t even find the contracts much less manage them.*” Reducing maverick buying and optimizing the value of new and existing contracts is a fundamental tenet of supply management organizations.

More and more companies today are moving the contract management responsibility to the supply chain organization rather than having it in legal, finance, or operations as organizations have come to realize the importance of contract management. A driving force of this movement to the supply chain organization is the need to ensure the contracts are collected and maintained in a central repository. Furthermore, the migration of the contract management function to the supply chain organization allows the supply chain leader to more effectively leverage spend particularly in the areas of services, where there is a greater opportunity for cost reduction and risk mitigation. And speaking of risk, sourcing decisions are demanding that a risk mitigation methodology be integrated into the decision tree process. Not only are price, value, and quality primary considerations, but an additional factor is the risk element. Best of class organizations are developing and adopting sound methodologies that include: (1) identifying all of the risk elements, (2) prioritizing the risk, (3) determining the

probability of the risk to occur, and (4) assessing the dollar impact to the sourcing decision if the risk actually takes place.

**9. Reduce company-owned inventory.** With key suppliers in place and delivering against their contracts, supply chain organizations should strive to constantly review their inventory levels and to keep them at an optimized level. More so today than in the past, the Chief Financial Officer has put Inventory on the radar screen and the financial team is constantly looking for new ways to improve the bottom line and reduce working capital. Supply chain teams often begin by defining the “real” cost of holding that inventory. This cost is often higher than the generally assumed 20% to 25%. In fact, ISM has compiled documentation to indicate that inventory holding cost could be up to 40% or higher of the cost of the item. Best of class companies today are placing more emphasis on demand planning and forecasting as just one additional means of ensuring that inventories are optimized. Poor planning and forecasting is a direct cause of inventories that are out of balance with the business needs.

**10. Green Initiatives and social responsibility.** Greening the supply chain is about reducing the carbon footprint of the supply chain. The trend and forecast is that carbon rights will be established in the U.S. We are already seeing organizations such as Dun and Bradstreet producing reports that reflect “green” companies. More and more RFP’s are being generated asking suppliers and service providers to provide information on their green initiatives.

Social responsibility is a “framework” of measureable corporate policies and procedures that result in behavior designed to benefit the workplace, the individual, the organization, and the community. Social responsibility is playing an increasingly significant role in the supply management organization decision process and risk, for both the buyer and the seller, will become apparent for NOT having a Social Responsibility program.

## **SUMMARY**

The ten best practices described above represents a framework of strategies and best practices that best of class supply chain organizations should strive to achieve. One issue at hand is that over the past several years, we have witnessed a changing market environment and that our effectiveness as supply chain organizations revolves around short term flexibility with long term maturity. And we must remain flexible in prioritizing these initiatives in order to meet the challenges of the day. To achieve supply management excellence, we feel that these identified best practices provide a valuable roadmap for organizational effectiveness.

## **REFERENCES**

### **Book references:**

Riggs, David and Robbins, Sharon. *The Executive’s Guide to Supply Chain Management Strategies*, AMACON, A Division of American Management Association, New York, New York 1998

### **Journal and magazine article references**

Aberdeen Group, *The Contract Management Benchmark Report*, June 2003 Satellite Seminar, *Controlling Cost by Controlling Your Inventory*, April 2004