Purchasing Professionals Are Making Everyday and How You Can Eliminate Them By Becoming a World Class Purchasing Professional!

By Omid Ghamami
THE Godfather of Negotiation Planning

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
About Omid Ghamami

Omid Ghamami is President & Chief Consultant at Purchasing Advantage, a purchasing seminar and training solutions provider. Since 1995, he has taught thousands of hours of courses, workshops, and seminars in 10 different countries on topics related to the entire spectrum of purchasing, supply chain management, purchasing contract law, negotiations, and supplier management.

Omid holds a Bachelor’s degree in Business Administration with a concentration in Finance and a minor in Economics from California State University, Sacramento, as well as an MBA from the University of California, Riverside (Class President).

Omid has 18 years experience with Intel Corp, where he rose to the position of leading their entire global corporate purchasing operations organization. His experience and strength in negotiations earned him the corporate designation of “Godfather of Negotiation Planning” for the entire $2.2B global purchasing organization.

Omid is also an esteemed Adjunct Professor of Purchasing in the Los Rios Community College District, where he has pioneered the development of an innovative purchasing curriculum that is the first of its kind in the California community college system and has received many accolades.

He has broad and rich experience in complex, high dollar value, and high stakes negotiations, total cost analysis, supply chain management, purchasing contract law, purchasing operations, purchasing policies and procedures, complex sourcing strategies, controls and risk management, selection and deployment of purchasing systems/tools, purchasing integration of mergers and acquisitions, international purchasing strategies, negotiating with different cultures, supplier performance management, and purchasing strategy mapping and execution.
Dear Friend,

You made a smart move because only a small percentage of Purchasing Agents around the world have this very special document and the follow-up training.

You see, in my travels around the planet, meeting with, listening to and working with thousands of Purchasing Agents, as well as my own observations running global purchasing operations at Intel Corporation - where I worked for nearly two decades, I’ve identified the top major pain points that Purchasing Agents have to deal with on a daily basis. To call them a pain in the butt is an understatement.

I’ve isolated the top seven of these major pain points and am going to give you a paradigm shift from the old way of thinking to the brand new, highly regarded, intellectual approach that will put you light-years ahead of the pack while you actually have fun, get to enjoy this profession and put yourself in position to advance your career to much higher levels very quickly.

My intention is to lay out and analyze these major pain points for what they are, (I’m sure you know of them and many more) show you how you can easily overcome them, kick them to the curb and finally start enjoying one of the greatest and most rewarding professions in the world.

This report is just a primer to get you thinking about the right things. As we progress, what you’ll discover will be unlike anything you’ve ever read, been taught or learned about our business. You’re going to have lots of ah-ha moments and monumental breakthroughs.

You’re going to become a world-class Purchasing Agent. It’s not hard but it’s going to take a little effort to keep an open mind and pay close attention to what I present to you. Once you ‘get it’, I promise you, you’ll never look back.

Enough of doing what everyone else is doing, following antiquated systems and theories that never really worked! It’s time for you to grab the bull by the horns and tame the beast because as the wise saying goes:

“For if you keep on doing what you’ve always done, you’ll keep on getting what you’ve always got!”

I look forward to helping you take this quantum leap forward!

Let’s get started!
The Top 7 Deadly Mistakes Purchasing Professionals Make
And What You Can Do To Eliminate Them

1. Managing Rogue Internal Customers

Perhaps the most frustrating part of being in purchasing is finding out that the internal customer has already cooked a deal with a supplier, and then you have to figure out how to still add value to the process. Making matters worse, you have to slow down or even stop the process to exercise due diligence, which reinforces the perception that purchasing is a roadblock. These “after the fact P.O.s”, as they are often called, are the source of endless heartache and a big pain in the rear for all of us in purchasing. We live and breathe this problem, and I hear it over and over from purchasing professionals from different companies.

Do you ever wish there wish your company had a firm policy or tops-down directive with consequences for end users who circumvent purchasing and engage in rogue buying behavior? I have yet to find a company that has actually been willing to do this with any sense of conviction. Every company executive will say it is wrong and they are against it, but no company is actually willing to put a hard and fast POLICY (not a guideline, but a policy) with consequences in place. As a result, purchasing has no choice but to try and educate and motivate customers to work with them, forcing purchasing to do educational roadshows, newsletters, presentations, etc and the like to get the customer on their side – and even then there are no guarantees. What I have seen in different companies across many industries is that, on average, 90% of the suppliers get only 1 purchase order a year. This tells me that supply bases everywhere are growing based on rogue customer purchasing habits. How can we overcome this huge set of challenges?

I’ve noticed that this lack of directive doesn’t seem to apply to other internal service providers inside most companies. Almost all other internal service providers are given the right and expectation to put out mandates. We see it all the time. There will be an announcement in your company’s intranet site stating “starting Monday, this is the new human resources process for ____________”. There may be educational sessions and communications, but they will be fewer in number, more broad in terms of audience participation, and they are not meant to influence employees to get on board and partner together; they are instead meant to tell employees how things will be. Think about that for a minute. How much easier would our jobs be if purchasing could do this?

From expense report policies to airline travel policies to employee benefits policies to everything else, company practice mandates, saving the service organization sponsoring these policies the headache of having to influence employees to get on board. I think that a big root cause is that at the senior executive level,
purchasing is not understood, or it is viewed like what it was in the 1970’s – an overhead function whose primary job is to expedite the purchase of materials and services on behalf of the internal customer. When these executives look at purchasing cost savings roll-ups and reports, they ask themselves "If purchasing is saving us all this money, how come there is not that same amount of money left over in the company’s budget?" It’s enough to make us all scream!

There is a trickle-down effect of all of this on us as purchasing professionals of course. There are substantial amounts of money left on the table due to these after the fact P.O.s, to which purchasing can often add little value. There is the growth of the supply base that takes place as a result, which dilutes our efforts to aggregate expenditures to a smaller set of strategic suppliers. There is the time you spent on educating the customer, which as stated above no other internal service provider inside companies needs to do to this extent. There is the additional time and money you spend adding suppliers to the company’s master supplier database, and the additional time associated with physically placing the order. There is the additional time you’ve spent managing one more supplier, and also later spent trying to reduce the supply base, to likely include this after the fact P.O. supplier. There is the time taken away from being able to better prepare for, and therefore produce better results on, more large scale negotiations that you need to be getting to and should be focusing on. Lesser results in major negotiations on your part then invariably translate into slower career progression - because the root cause is viewed as your personal capabilities, instead of the circumstances you’re finding yourself in. And because 99% of major companies do not have a Chief Purchasing Officer (or variant of that title) sitting on the CEO’s staff, there is no voice at the top telling the executive staff of that company that this way of doing business is costing the company money and things need to change. The closest person to that role is the CFO (Chief Financial Officer), and they are the ones wondering why all those purchasing savings aren’t left over in the corporate budget!

Purchasing can fix these problems by operating smarter and with greater influence, with mechanisms in place to ensure that customers are on board - not because they have to be (the stick), but because they WANT to be (the carrot). We don’t need to wait until all the executives “get it” and publish internal mandates. Top spending customers need to be focused on, big wins tracked, and select customer representatives need to be made purchasing ambassadors so that the burden is not all on purchasing to make the model work. Savvy purchasing professionals are able to use these early engagement and influence mechanisms in a way that is both minimally time consuming and generates better results. The challenge is getting out of the fire and putting these proactive measures in place. It takes some upfront investment, but the heartache, frustration, and time saved on the back end, along with the career growth it can generate, is priceless.
2. Establishing Purchasing Value for Management & Customers

We are in one of those positions where we can go home at the end of the day knowing we have made a tangible difference – lower costs, better supply line, better contracts, better suppliers, better quality, better service – yet still have a hard time quantifying all of that for management and internal customers. From my perspective, the worst feeling is having spent a week being completely mired in what feels like value added activities, only to later find oneself struggling to know what to write in the weekly status report. The only metric that most everyone seems to understand is direct cost savings (those savings directly associated with negotiated price reductions), but even that is difficult because customers spend the residual money saved on other items, thus leaving senior management scratching their heads and wondering where all these purchasing savings are accounted for in the bottom line if in fact they are so plentiful.

Indirect cost savings (non-price related savings) and cost avoidance (elimination or avoidance of a cost or cost line item) are even more difficult for most buyers. Buyers often don’t know how to recognize or calculate them, so they often make the career limiting move of not capturing them at all! For instance, a warranty is negotiated to be 3 years instead of 2 years – how are the indirect savings captured for that? How much savings? Lead-time was reduced from 4 weeks to 3 weeks, resulting in reduced inventory requirements – once again, how are indirect savings captured? Some bells and whistles are pulled from the specs for a product, is that considered a cost avoidance? Is there a standard formula for determining indirect and avoidance savings? If so, where is it? If it doesn’t exist, how can these cost figures be justified to management and internal customers? If I report and track them, will these figures pass an internal audit? There are many such questions that buyers are faced with when trying to capture their value to customers and management.

The most frustrating situation that I often see is where a company’s management chain doesn’t recognize any savings other than direct savings (those related to purchasing negotiated price reductions), and so rolling up indirect and avoidance savings isn’t an option at all! In these situations, the purchasing department really never has the chance to capture and express their full value, and indirect and avoidance savings opportunities are less sought after as a result as well. It unfortunately becomes a self fulfilling prophecy. Rarely is this decision made by someone in the purchasing ranks however. It is almost always made by someone in the finance or accounting chain, as they have been trained to only track and report “hard costs.” This kind of reporting or influence structure in the organization is often problematic for purchasing. Reporting to the customer group itself, which happens more often than you might think, also creates similar sorts of challenges for purchasing professionals. It in fact could qualify as a conflict of interest - your customer, whom you are supposed to challenge and influence, also writes your performance review and pays your salary. Do you really want to bite the hand that feeds you? What a mess!

My best estimation is that purchasing professionals spend on average 75% of their working hours in pure fire fighting activities. Fire fighting to me means spending valuable time and energy on unplanned supplier or customer problems of some sort that do not add to TCO results in any way. These activities are very hard to capture in any meaningful fashion by purchasing professionals. How can they be? It’s like an airlines company taking credit for how well they handle emergency landings that they encounter many times a day. The focus goes straight to why there are so many emergency landings (as it should) instead of how well the

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
airlines handled them. Examples of fire fighting problems that can arise on a daily basis include a supplier who hasn’t been paid, an order that needs to be placed urgently, a shipment that is delayed, a customer who is upset about something... anything, an employee who is upset about something... anything, an after the fact P.O. that has come in, a supplier who has taken direction from an internal customer on something purchasing related instead of from you, and to be honest and perhaps politically incorrect, supporting procurement initiatives of the month from well intentioned but purchasing inexperienced senior management that are based on business journal fads and trends rather than proven total cost oriented objectives that have and will stand the test of time.

The goal is to structure workload and activities to get out of the frying pan and rise above fire fighting activities, and to use that time for more value added initiatives that have measurable and tangible results. We do this by throwing out the current reactive model of “management by distraction” and replace it with one that focuses. This takes a very coordinated and strategic effort that is based on models that are proven to work for purchasing professionals. This is not just theoretical, this is something that can be done, and I’ve personally mentored and watched such transformations that happened in less time than you would believe. From there, a set of pretty indisputable performance metrics can be tracked and reported that help support purchasing’s value add, which also helps boost career results, eventually having pretty dramatic impact on personal income. There’s no reason why every purchasing professional can’t make this transformation. On top of being good for your career, it’s also very personally enriching and fulfilling.

3. Meeting Supply Base Reduction Targets

All of us as purchasing professionals are challenged to reduce the size of the supply base. After cost savings, it’s one of the biggest metrics we are held accountable to. And for good reason. The more our expenditure volume is diluted over a larger base of suppliers, the less negotiating strength we have, and the more time we spend chasing after a larger and larger base of suppliers. More contracts, more negotiations, more hassle, more supplier excursions... more everything but cost savings! The problem is, even as you make specific efforts to reduce the supply base, more suppliers are creeping in like clockwork. The culprit is all the low dollar transactions that fly below our radar as purchasing professionals. They are the ones that are doing a lot of the damage.

However, if you think customers are the only problem, you need to look back at your own purchasing organization! Data entry clerks are inadvertently increasing the supply base, or at least making it look larger than it really is. For instance, if you want to find “IBM” in your corporate supplier database, here is what you can expect to see:

1  I.B.M.
2  IBM
3  IBM, Inc.
4  IBM Corp

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
There could be 30 or more entries for the same company in your master supplier database! This is most often the case, because little attention is paid by the data entry clerk who is adding a vendor for payment. If they don’t see the exact company with the exact same address, they typically don’t hesitate to create their own entry for this company to get paid. So it seems we have forces from both ends increasing the supply base metric that management so eagerly wants to see reduced!

I have sat and watched purchasing professionals manually reduce the supply base. There’s really no other way, but it’s about as fruitful as trying to kill ants one by one. The process entails going into your company’s master supplier database – and we already know what a mess that will be - and trying to clean it up. Here’s the drill – we want to get rid of suppliers, but not ones that will have the risk of a p.o. coming in next week for, only to have them added again. So which ones get deleted? Answer: the ones that haven’t been used in a couple of years or so. In other words, the suppliers that were effectively not part of the supply base anymore anyways, but are still lingering on the supplier database in name only. By removing these historic suppliers, we are changing management perception (by improving the supply base size metric that management looks at) but we are not improving reality (the number of active suppliers with whom purchasing is diluting their expenditure volume) in any way. Is this really where we want to spend our time? Hours and hours just to manage perception, meanwhile reality hasn’t improved in any way? What are we trying to accomplish anyways?

The first thing you need to do is to stop spinning your wheels by even caring about the supply base size. Read that again. What I just said is considered sacrilege in the purchasing ranks, and I’m sure that this is the first time you’ve heard someone say that -- which is why I had you read it twice to make sure you didn’t misunderstand. Let me reassure you, you didn’t misunderstand at all. Just in case, let me say it again: you need to stop caring about the supply base size. It’s irrelevant! It’s irrelevant for the reasons I stated above (duplicate entries, historic supplier entries lingering around), and for many other reasons. You have to step back and remind yourself what problem you were trying to solve to begin with: avoiding the dilution of money across too many suppliers, and avoiding the wasting of your time and customer time on too many suppliers.

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
That is the goal, and nothing else. You are improving neither of those situations by getting rid of oldy-moldy suppliers in the corporate supplier database that aren’t getting any of your business and haven’t in a long while. So what you really need is a new metric, one that measures what you are trying to accomplish, because the other one (supply base size) only measures management perception. So why not improve reality too?

The new metric you should be focusing on is where 90% of your spends are going to. In an indirect materials environment (which in reality is where all the undesired supply base growth is happening), 90% of your spends should be going to 5% or less of your suppliers. THAT is your metric. If you can achieve that, then you know that you are managing the company’s money effectively, and that is the real goal that management is trying to achieve, whether they know it or not. Of course this presumes that these 5% of suppliers are under contract with negotiated prices and terms, but even if they are not, now you know who they are and what you need to do! It makes our jobs much easier when the work is laid out for us and isn’t overwhelming (such as with the case of trying to reduce the supply base by thousands). If you have 90% of your spends going to 15% of your suppliers, then you need to reduce the # of strategic suppliers you have that are getting the bulk of your spends. We are talking about focusing on a handful of suppliers. This is far easier and has far more strategic TCO impact than pulling your hair out trying to reduce the supply base by thousands on the back end.

By focusing on this metric, all your behaviors will change too. You will stop focusing on the suppliers that don’t matter and you’ll start focusing on the ones that do. Supplier business reviews, score cards, performance management – all of that needs to happen with this small set of suppliers. The rest of the supply base will become increasingly irrelevant, which is exactly what you want. And who cares if the supply base number is still large? That’s not a good measure of success anyways. Funnel money to the big boys and these small suppliers will fall off your corporate supplier database on their own.

Making this model work right requires a lot of work and strategy, but at least it will be time well spent; time spent that will influence both perception and reality. As purchasing professionals, we can make all the difference. Start with changing your metric, and then change your focus to your strategic suppliers. Watch your flowers blossom while the weeds effortlessly wither away on their own. We can’t ask for any better situation than that.

**4. Finding Time to Both Place POs And Negotiate Contracts**

Probably the hardest part of what I do is talking to purchasing professionals who are flustered because they can’t get to the strategic parts of their job – negotiations, supplier management, benchmarking, etc – because they are too busy placing purchase orders…. something the department administrative assistant could probably do. It’s hard because I feel for them, and I understand their pain and the reasons why completely. They really are in a bind.

The pain doesn’t stop there. Placing orders is an unappreciated function. Nobody notices when you get everything right, because they expected you to get everything right. If you make a mistake though (such as inputting the wrong quantity, price, product, supplier name, supplier address, etc.), everyone notices.
“Where’s my product?” “Why did I only receive this many units?” “How come the supplier kicked the PO back? “You forgot to include _________ on the P.O.!” These are all communications that signal a bad day in the life of a purchasing professional. On top of that, it is a career limiting function. Nobody ever went on the fast track to becoming the next director of corporate purchasing because they were so good at placing purchase orders.

What’s even worse is that when you have one of these hybrid positions (where you are responsible for both supplier negotiations and placing purchasing orders), you are usually completely qualified to exclusively do supplier negotiations as a full time job. However, since management cannot justify adding full time headcount to just place purchase orders, the only way out for them – that they can see anyways – is to have their buyers also place orders. So what happens next? The outcome is predictable. Look at life in the purchase order placing business: The purchase orders are urgent, all of them. There’s no such thing as a customer that doesn’t care when they get their items. Their lack of planning becomes your emergency, and this will translate into a number of emergency purchase orders every day. That means everything else needs to get dropped, which ironically includes the strategic negotiations activities you so desperately want to get to that have the ability deliver such great TCO results to the organization!

And you have contract negotiations to get to. Those can’t fall off the back burner either. However, what does fall off the back burner, not by choice, is all the preparatory requirements to ensure great negotiation results. Should cost models, must cost models, total cost models, benchmarking, negotiation strategy development, customer alignment on BATNA (Best Alternative To a Negotiated Agreement), etc all fall by the wayside. Why? Not because you don’t think these things are important, and not because you don’t want to, and not because you don’t have the skills or capability. It all comes back to time. There is no time. The purchase orders keep coming, customer emergencies keep happening, and before you know it, there’s no time left to do anything else. So what happens? Well, you wing it. You do the best you can with negotiations with the time you have left. And given those circumstances, you’re probably producing pretty good results, but guess what? We both know those results would have been a lot better if you didn’t have those pesky P.O. placement responsibilities on your back.

Fast forward to your performance review. Uh-oh. All you really have to show is that you managed to keep your various customers happy by placing all their purchase orders in a timely fashion (translation: you dropped everything to handle their daily emergency orders), and you had a few decent cost savings here and there. There is really nothing compelling in your performance review that say “this person is ready to do negotiations full time” or “this person’s ready for a promotion”. Instead, what management sees is “this person can’t get very good negotiation results on a part-time basis, so why would I have them do it full time?” What you have is a very ugly and undesirable vicious circle: the more you place orders, the less you are able to focus on strategic purchasing activities, and the less you are able to focus on strategic purchasing activities, the more management is inclined to keep you placing orders because of your lack of results in strategic purchasing activities. Another consequence of this is that your manager likely won’t have enough ammunition from your cost savings results (or those of your similarly challenged peers) to take to his or her management chain and justify more headcount to just place purchase orders so that you can focus exclusively on strategic negotiations, so you are stuck again. How can we get out of this cycle of pain?

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
Luckily there is a process that works to get us out of this cycle, without having to switch companies. This involves an agreement with your manager to let you exclusively negotiate contracts for a period of time, using those results to justify a different business model that takes P.O.’s off your plate forever. However, securing this approval requires preparation, and actually getting the results requires that a well defined set of steps are followed exactly for best results and highest probability of approval. I have done this successfully many times with purchasing professionals who were stuck in this situation and desperately wanted out.

What you need to know is that complacency in this situation is a career and morale killer. I’ve been there, and a couple of decades later, to my amazement, I still see it all the time. That’s why it’s so painful for me – people aren’t seeing the solution, and it’s not that far off. Handling this right can make all the difference in a purchasing professional’s career, one that doesn’t have to be frustrating and one that can be very lucrative and fulfilling by following the right steps.

5. Trying to Meet Ever Increasing Cost Savings Goals

Cost savings. That’s where it starts and ends for all of us in purchasing. Management can introduce 100 flavor of the month programs and metrics that need to be adhered to, but at the end of the day, we are expected to excel in delivering bottom line TCO to the company. When I first started in purchasing many years ago, cost savings was the only performance metric being tracked! Now, a sophisticated purchasing department will have well over 30 – 40 metrics that are being tracked beyond cost savings, and purchasing professionals are expected to perform to all of them. Green initiatives, small/minority/women owned business support, Sarbanes-Oxley legislation compliance, supply base reduction, on time delivery, customer service scores, safety excursions, public relations excursions, new systems/tools implementation, government requirements compliance, and on and on. The problem is that the number of mandated purchasing metrics keeps increasing and the cost savings expectations/targets keep increasing as well, but meanwhile the number of department purchasing personnel is decreasing or at best staying the same!

What adds to the challenge for all of us is that failure to meet expectations in all those non-cost savings metrics will result in a bad performance review, but performing very well in those areas will not lead to a good review! Only great cost savings results will result in a good review, assuming you met expectations in all those other 30 or 40 metrics. So as it turns out, you don’t need to perform outstanding in the non-cost savings metrics, you just need to perform *good enough*. This is a really important distinction to understand, because much time can be misallocated trying to exceed expectations in an area where you are only rewarded if you meet expectations. Read this out loud three times: *No matter what management tells you, the only area we get rewarded for exceeding expectations is cost savings.* Back to what I said earlier – that’s where it starts and ends for all of us in purchasing. So it’s no surprise that those purchasing professionals that let themselves get mired in all of the metrics presented before them by management often find themselves flustered and unproductive. It’s like trying to be the captain and the cook of a ship at the same time. The food only has to be *good enough*, but the top priority has to be steering the ship safely and efficiently in the right course, all the time. Try to excel at both, and you will fail at both. Excel at the food but take the wrong route, and you will still be viewed as a failure. Maybe that’s how the Titanic crashed, who knows? The only way to succeed in this model is to excel at being the captain while ensuring the food is just *good enough*. The same is true
with cost savings and all the other purchasing metrics. You need to excel at cost savings, and the rest of them just need to be good enough.

This doesn’t solve all the problems for us though. There is still the issue that we are being asked to hit higher goals and then later, stretch goals on those higher goals every year for more and more savings... from the same suppliers! Now put yourself in the supplier’s shoes for a minute. When purchasing comes to the supplier and asks for a lower price, what does the supplier hear? The supplier hears “we need you to make less profit so we can get a lower price.” Despite its commonality, this is actually a pretty unsophisticated purchasing approach to cost savings, and it is decidedly win/lose from the supplier’s perspective. And it’s easy to understand why. There is a whole supply chain worth of costs that can be focused on, and the purchasing professional focuses squarely on supplier profits as the only opportunity. Is this the best we can do, and is this in the spirit of long term supplier relationships that we talk so much about? After all, we have to care about our supplier’s pain points if we want to try and solve our own as well. There are so many TCO opportunities left unturned when all you focus on is the supplier’s profit margin.

Most commodities or category areas don’t offer enough savings to “keep going back to the well” with the supplier. The Information Technology (IT) commodity is probably the only exception. Like clockwork, we can expect that the price of existing products will have supplier profit margins that are ripe for analysis and negotiation. I remember once sitting in a commodity strategy review meeting. Every commodity manager stood up and talked about their results from the previous year, and their plans for the upcoming year. The Information Technology commodity manager proudly proclaimed that he had achieved 25% cost savings in the prior year. The director of corporate purchasing then quickly brought him down to earth, and I suspect maybe lower, by saying “Big deal. That’s like falling off a log with your commodity.” Ouch.

However, as we are all aware, the rest of the traditional commodities (non-IT) don’t generally have these kinds of huge annual cost savings opportunities. Take GSS – General Site Services – for example. The cost of labor, chemicals, and other site service costs are not going down for sure. Next up, external workforce. Contract and consultant labor is fairly constant. The same is true with construction services, both from a labor and materials perspective. In fact, especially with China and India buying so much concrete and steel, the cost of materials is on the upswing. Then you have the human resources or employee benefits commodity; insurance (medical, dental, health, life, etc), relocation, retirement plans, etc. The cost of all of those, especially medical insurance, are on the rise on an annual basis. There are still other commodities (marketing, capital equipment, manufacturing consumables, direct materials, etc), and all of those are on the rise, with the exception of certain direct material commodities and manufacturing consumables, which remain vulnerable to price fluctuations in either direction. In short, unless you are managing the IT commodity or riding an infrequent temporary wave down on certain goods or services, you are very likely going to a well with already pretty low water levels.

So far I’ve told you what you already know – the aggressive cost savings targets you received from management aren’t going away, and your suppliers have gone through the “I need a better price” carousel many times already. How many times can you keep bidding out the business for a lower price? How many times can we ask the same suppliers to make less profit so we can hit our new cost savings goals? Is this really the only trick we have up our sleeves? Reverse auctions were supposed to be the answer, but in reality, it
only automates the process of zeroing in on supplier profit margins. On top of that, it is an extremely stressful process for suppliers to battle it out in a war-field to see who is willing to live with the lowest profit margins of all (makes me wonder if this is a war that is even worth winning), with the alternative of no business at all. Is this really the way we want to build long term relationships with suppliers, which we talk about so often?

The good news is that there really is a silver lining to this black cloud. Take a look at this supply chain pictorial. All the unnecessary, duplicate, and excessive costs in the supply chain are contained within and between the linkage points in this graphic. However, when we go to a supplier and say “I need a better price”, all we are really focusing on is the little circle in yellow, representing supplier profit margin. Look at all the other opportunities that are completely ignored!

As purchasing professionals, we can make all the difference by expanding this focus in the yellow circle to encompass a larger piece of the supply chain, looking for corresponding cost savings opportunities with a broader focus. **This is the secret to achieving break through cost savings results.** The entire supply chain cannot be focused on without significant supply chain systems, processes, and communication models in place. I can pretty much guarantee you that your company doesn’t have those things in place across the supply chain - and you don’t have time to wait. However, the circle can still be expanded to include at least two full supply chain components, without needing any special supply chain systems, tools, processes, etc.

There is a five step methodology I teach and have supervised very successful implementation of. The very first step is completely changing our paradigm from reducing price to reducing supply chain costs. I remember working with a company on this exercise, and we identified that their specifications required that the piping built by a supplier had to have the customer’s company name stamped on it every 3 feet. This turned the pipe from a standard product to a custom product, adding tremendous cost. Where was this piping going? UNDERGROUND, where nobody would see the stamping. We got rid of the stamping requirement and saved 10%. 10% savings – Bam, just like that. That’s a lot, and the supplier was happy to be out of the pipe stamping business, and their profit margins didn’t have to take a hit. Lead times became a lot shorter too, since there was now a shared inventory model at the supplier, as this was now standard product that their other customers were buying too. The purchasing professional was thrilled as well to be able to get what felt like a free windfall of savings. This is just one of hundreds of examples of ways to take costs out of the supply chain, and again, this was done without the need for elaborate supply chain systems, tools, standards, or communication models.

This model is carried out and proven with one supplier, then expanded to other top expenditure and critical suppliers that the purchasing professional works with. This approach above is the key to getting world class cost savings, year in and year out, without focusing on wringing the supplier dry of any profits they might be

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
receiving. It’s important for all purchasing professionals to recognize this opportunity and receive the training and practice to make this transition. It will require selling suppliers and internal management and then driving execution. It’s not a major hurdle to jump, and there is a huge pot of gold waiting for us on the other side. The alternative, as we discussed earlier, is not so attractive…

6. Internal Audit Visits and Business Process Compliance

We’ve all done it. We get word that internal audit is coming to town, and we scramble to get all our files in order so that we can best convince the internal auditors that there’s nothing to see here, and they should keep moving along. It’s like trying to cram in a year’s worth of flossing right before your annual dentist appointment. I’ve done that before too (side note: many cavities later, I now floss regularly). I have a friend who exercises like a mad man and eats almost nothing, both the day before (and only the day before) he gets his annual blood tests done. Why? Because he wants his results (blood sugar, in particular) to show lower than they really are. Sure enough, his blood sugar results come out showing normal. Who is he trying to fool? Does a passing set of results under such circumstances really mean that everything is in check, and that there is something to feel good about if the results are good? Its no different when you scramble to get things in order before an internal audit review.

Part of the challenge is that we don’t know what to expect when internal audit rolls around. Internal audit is almost never comprised of former purchasing people, so it’s a bit of mystery as to what their findings will be. The other problem is that their findings, once finalized, are binding. It’s almost as if the IRS has contacted you and wants you to get back to them with some key information: Closing the loop is not really optional. So what is internal audit looking for, anyways? Well, they really care about two things at the end of the day: doing business legally and doing business smart. It gets much more detailed than that, but if you want to boil it down as much as possible, those are the two things they care about.

Internal audit is pretty well trained and qualified to make solid assessments regarding their first area of focus (doing business legally), and I have only once personally seen this be a major issue in a purchasing department that I was working with. There was a Fortune 50 company that had top to bottom corruption happening at their Philippines site, which employed thousands of people. There were so many kickback schemes going on that it was just incredible. For example, this manufacturing company had 10,000 days of inventory of hairnets at that facility. Why so many? Simple. Hairnets cost very little, so they were not hitting anyone’s radar in the approval loop – not finance, not management, not purchasing. They were small dollars and they were a necessary item for employees on the manufacturing floor. So what’s the problem? Well, commercial hairnet comes in big boxes that take up a lot of room, so much room in fact that this company had to lease 3rd party space to store these and other over-ordered items. The kickback scheme was pretty sneaky. It was between the company that owned the 3rd party space and the person who kept ordering endless hairnet boxes and filling up the leased space with them. There are many more examples that I have from this case (the whole Philippines organization for this company ended up getting shut down in fact, in no small part due to these wholesale excursions), but the point remains – while infrequent, these things do happen. However, the fact that you’re reading this report indicates you are trying to make things better, not worse, so let’s assume that this piece doesn’t apply to you. Onto internal audit’s other focus area: doing business smart. This is probably where you are experiencing most of your pain.

Copyright Omid Ghamami ~ www.PurchasingAdvantage.com
Doing business smart can mean a lot of things. It includes efficiency, effectiveness, and safeguarding of assets. And while breaking the law or company policy is pretty black and white, the areas above are not so clear. They are mostly subjective, meaning, they are subject to the opinion of the person doing the analysis. And we already established that internal auditors almost never have a background in purchasing. This spells trouble. Just imagine if you were an internal auditor. If you audit an entire organization and can’t come up with any findings, it doesn’t look good. It’s like being a police officer who can’t find anyone to give tickets to. Every group audited by internal audit will have findings; it’s just the way it is. Therefore, the internal auditor is looking for what they can hang their hat on and say “aha, there’s something I can do a write up on.” They will ask leading questions in employee interviews, and sometimes they will just let you talk until they catch you saying something that raises a flag for them. Fair enough, but the problem is that they really don’t understand our business, and what can often happen as a result is both heart breaking and maddening: your department manager ends up agreeing to a report that calls for a series of actions and controls to be put in place that are technically correct but are the wrong thing to do for the business. We as purchasing professionals, while not trained as well as internal audit in audit theory, are much smarter than internal audit in terms of knowing what does and doesn’t need to be fixed in our respective departments – but who’s going to tell that to internal audit?! Instead, we’re stuck implementing all these action items that slow the business down and make it even harder to focus on trying to get results. How can we overcome these challenges?

We need a way to work with internal audit that doesn’t require a mad scramble before they come, and worse yet, then having to implement a set of internal audit report requirements that are theoretically correct but in reality completely impractical for the business. Making this more difficult is the fact that internal audit by design has an arms-length distance from the company, acting as third party auditors, which precludes collaboration, because it is a conflict of interest for them to do that. So are we stuck in internal audit jail as purchasing professionals? Are these audit reports a necessary evil in our business model? How do we go back to “business as usual” without these huge distractions that come with internal audit visits?

It’s not all bad news though. All of this heartache is preventable - it really is. The scrambling preparation, the implementation of impractical internal audit report requirements, etc. All of it, throw it all out the window. This is a big waste of time for all of us in purchasing, and it is completely avoidable. What we need to do is something called a risk assessment. It involves assessing all risks inside our respective departments, as well as the corresponding controls. Each risk can be classified by impact and probability and each control can be classified by the type of control it is (there are four different types). This risk assessment will define both existing and to-be controls in the department, based on identified gaps that need to be closed. The goal is not to eliminate all risk (which is impossible and impractical), the goal is to balance risk levels with the ability to have an agile department that is unencumbered by excessive process, approval, and procedural requirements. Think of your own daily life – if you wanted to eliminate ALL risk, you wouldn’t be able to drive a car (might get in an accident), cross the street (might get hit by a car), go to any area that is earthquake prone (might die in a collapsing building), etc. We make decisions about how to balance risk with the ability to run our lives in a productive fashion and we generally do ok. Purchasing departments are not a lot different.

So this risk assessment process sounds pretty difficult and complicated, right? Not really, not once you’ve done it. It requires some training and practice, but what doesn’t in purchasing? So here’s the beauty of the
whole process: when you do a risk assessment, **you are speaking internal audit’s language**. Remember, when internal audit comes to your department, they are trying to figure out *your language*, and then you lose all control of how they interpret things and what they conclude, especially since they are creating their own assumptions on how your business should be run - just what you need, right? However, if you speak their language, you regain all control of the process and the outcome, which is exactly what you want. The trick is to involve internal audit in the risk assessment process. They won’t actually participate, because they still have that arms-length requirement. But you can and should make them aware of what you are doing and give them a chance to provide input. In the end, you can have them look at the output and try to poke holes. You’ll never get them to “approve” the document – that darned arms-length thing gets in the way again – but you will get them to say it looks like a solid analysis, and that’s all you need! That is internal audit code language for - “we approve this document, but we just can’t tell you that we approve this document.”

Then what you do is you make the outcome of your risk assessment a part of your departmental standard operating procedure, and let internal audit know this was the case. This does two things, which are critically important. The first is that internal audit will have a much greater sense of comfort regarding your business. Their road-map of who to audit and when is largely based on perceived opportunities. If they think your backyard is in order, they don’t even visit. So that’s one big time saver – less face time with internal audit. The second big outcome is that when internal audit does come around, you dust off the risk assessment document and tell them to audit you **based on your own criteria**. Isn’t that better than letting them invent their own?? Now, they won’t agree to this (yup – you guessed it, that pesky arms-length thing again), but I promise you based on years and years of experience that they will breathe a sigh of relief that you have such a document, and they will do just that: audit you to your own risk assessment. No more scrambling, because you knew a long time ago what to expect. And then now, instead of this being an audit to ideas that internal audit comes up with regarding how you should be running your business, this instead becomes a garden variety compliance audit – where you are measured against **compliance to your own documentation**, and not to ideas or notions that internal audit comes to during their audit that may or may not be practical or even relevant.

Taking this approach, which will require specific purchasing risk assessment and controls training, is an extremely liberating exercise, and you will look like a hero for allowing the purchasing department to create a mechanism to get audited less often and to get audited to their own criteria instead of someone else’s. You can’t afford not to do business this way.

**7. Dealing with the Legal Department and Sticky Contracts**

You know the feeling well. It’s that pit in your stomach that you get when a supplier redlines your contract. You know the contract now has to go to the legal department for approval, which is where contracts go to die. That blasted legal department, why are they so slow and understaffed? That’s when things slow to a halt, and the lawyers go at it - but only when they are good and ready. There are a pile of contracts ahead of you in line, and the legal department does not share your urgency for getting things closed. Why did the supplier have to redline your contract? Why is the legal department so understaffed? What is going to happen to your negotiation timelines, and how are you going to explain this to the customer in a way that he or she will
recognize that this big delay coming up is not your fault? Why isn’t the legal department structured to respond to urgent contract requirements? How can we streamline or avoid this time sucking process?

Think about it from the legal department’s perspective for a minute. If you come with a rushed contract review requirement, they view that as no different as when a customer comes to you with a rush P.O. that you weren’t involved with upfront. And if they rush the review on your behalf and maybe don’t hold the line as much on certain legal issues, the upside is that they might get a color certificate of appreciation in a handsome cardboard frame. Meanwhile, the downside is they might concede on - or worse yet, completely miss - some very important legal issue which later ends up costing them their job or just stifles their career growth. Like I said, they will get to us when they are good and ready, and they don’t share our urgency.

The challenge here is that standard contract templates contain lots of terms that can be dangerous. The way our standard contracts are written are generally favorable to us more so than to the supplier. It only makes sense; our company is the one that wrote the standard template! Clauses such as those pertaining to intellectual property ownership, insurance requirements, indemnification, and the lack of reference to limitation of liability (which means there isn’t any limit to the supplier’s liability!) all can spell trouble once the supplier decides to take red pen in hand.

What’s frustrating is that the supplier may not do this until everything else has been agreed upon. You finish negotiating the pricing and pricing related terms, and then when you get to the contract terms and conditions…. reality hits.

The legal department is not really going to have the same objectives as purchasing. We know this going in. They are not looking for the best price, lead-time, warranty, quality, customer service, availability, inventory models, or anything else like that. They figure you’ve already taken care of all of that. They are looking for legal risk, and when they find it, they won’t sign off unless certain changes are made. It’s not worth it for them to rush a contract through with terms that may get them in hot water later just to help you with a time based emergency. They’re not going to do it, because like I said, they get paid for having zero legal excursions on their watch, not for delighting purchasing professionals with their flexibility and agility in reviewing contract terms.

That’s just one part of the problem however. The other part of the problem is that most purchasing professionals attach a supplier quotation or proposal to the back of a contract as an exhibit or addendum, call the contract complete, and move on with contract signature. Why is this even an issue? Isn’t that what we’re supposed to do? Well, it goes back to this simple fact: the contract is just a template, and it doesn’t “know” if you are buying toilet paper or nuclear warheads with it. Therefore, there are a lot of clauses that don’t solve all your problems, because the contract is just a piece of paper and it can’t possibly forecast your requirements for each transaction.

For instance, if your standard contract has a three year warranty clause and you are buying capital equipment for the manufacturing floor – great, you have three years coverage in case something goes wrong – wonderful, right?! Well, not so fast. The contract will not specify in what period of time the non-working piece of equipment will be repaired or replaced, meanwhile, you have manufacturing lines down due to this issue, and the manufacturing manager is breathing fire down your neck. The contract also won’t specify who
pays for an engineer to fly out if necessary and who pays for their hotel, meals, etc while they are there. The clock is ticking, the world is mad at you, and all you can point at is a contract that you thought gave you complete coverage for three years, only to find out that the supplier can take a month to fix the equipment and still not be in breach of the contract. If you don’t already know from experience, take my word for it that this is the worst visibility ever, and it doesn’t happen only to capital equipment buyers; it can happen to anyone who is buying critical items in purchasing (and what customer will say their items are not critical??).

I liken writing a contract to setting expectations with your kids. If you clearly state everything you want and need to see them do up front, then the likelihood of undesirable behavior afterwards decreases. However, if you don’t clearly set expectations up front, then you are going to spend all your time catching them doing things wrong on the back end, and it takes a lot more time to do that. That includes having common definition of things. If I tell my son to clean his room, his definition of his room having been cleaned is very different than my definition, so I have to go back after he thinks he is done, and tell him everything he still needs to do. It’s time consuming, and it’s frustrating for both of us. But guess whose fault it is? MINE! I didn’t tell him what my definition of a clean room was, so he used his own - who can blame him?

It’s no different with suppliers. The contract is your one chance to document every single aspect of performance expectations, and to do so in a manner that has teeth (consequences for breach of contract). When we don’t take time to do that, then that’s when we end up in that endless cycle of fielding customer phone calls because the supplier messed something up, and you won’t have anything to point to in the contract that says what clear and documented expectation they did not meet by their recent performance excursion. In other words, the supplier will be performing poorly, and there’s not a single clause in your contract that calls this out as a breach. Pretty frustrating, right? It’s a pay now or pay later process, and you may not know it, but you are spending a lot of your time paying later with your top suppliers, and it’s honestly not necessary.

So what can we as purchasing professionals do to overcome these kinds of contract challenges? The first thing you need to do is completely change your entire perspective about contracts. Contracts cannot be viewed as something the legal department owns or approves. That process is preventable. It’s preventable in three ways; one is to negotiate and interface with the supplier in such a way that they are either influenced or dis-incentivized not to redline the contract. There are a set of steps that I teach that need to be followed to do that properly. The second is to properly customize contracts up front to meet your situation specific requirements, resulting in far fewer excursions on the back end. The third thing is to stop saving the terms and conditions for last in negotiations – this is one of the biggest mistakes I see purchasing professionals make. When you save them for last, all the leverage has shifted to the supplier at that point, and they will redline the contract. And they will do so liberally, following which you will be put into the queue to go into the dreaded legal department black hole.

There are documented processes and methodical steps that must be taken in order to properly achieve the above. Once that is accomplished, contracts will shift from being a thorn in your side to actually being a great aid to achieving world class results in much shorter negotiation time frames. It’s one of the most liberating experiences you can ever have in our profession. You won’t need the legal department any longer, and the contract will be the reason why you are successful instead of the reason why you get bogged down. Pretty
soon you will be a high performing internal consultant to your peers, and that gets attention and spells promotion. I know, because I went through that exact cycle, many times. Follow my lead on these areas and you’ll see what I mean. The results are a blast, and your career will get a big boost.

Now that we’re both on the same page, stay tuned for my follow-up emails to this Report. In the coming days, you’re going to learn how you can virtually eliminate these seven mistakes, separate yourself from the amateurs and become a Pro caliber, world-class Purchasing Professional, playing in the big leagues, working smart and reaping big time rewards, personally and professionally!

Best Regards,

Omid Ghamami
President & Chief Consultant
Purchasing Advantage
www.purchasingadvantage.com