

Driving performance and value through strategic vendor management

As companies face increasing pressure to reduce costs and improve productivity and efficiency, many are looking to outsource functions and leverage third party vendors. As a result, large organizations often have hundreds of vendor relationships to manage. Increasingly, these relationships are drawing scrutiny from regulators, boards of directors and internal/external auditors. With this increasing dependence on vendors, it can be challenging for organizations to effectively monitor and manage these relationships.

Organizations seeking to realize the intended value of their outsourcing arrangements must take a holistic look at their vendor relationships and develop an effective vendor management program. Leading organizations are implementing Vendor Management Frameworks to provide structure, consistency, accountability and controls over vendor management activities. The framework forms the foundation from which vendor management activities are driven by linking strategy, policies and processes together. The framework would generally consist of the following elements:



Vendor Management Strategy

Establishes the context, strategy, objectives and guiding principles upon which the framework is based.

Vendor Management Policy

Defines the expectations and policy requirements of the framework.

Governance

Articulates organizational structures and reporting lines for the day-to-day execution and management of vendor management activities.

Process and Controls

Describes the activities through which the policies will be applied, defining process flows, accountabilities and activities to ensure that vendor management activities are conducted in a consistent manner. Identifies critical vendor management risks and controls for managing these risks.

Roles and Responsibilities

Communicates the specific roles and responsibilities of all stakeholders involved in the vendor management lifecycle.

Performance Reporting

Defines the reporting standards, tools and templates to be used to monitor a vendor's performance and ongoing viability, identifying emerging vendor specific risks and enforce vendor management activities.

Enabling Technology

Outlines the systems and infrastructures required to enable vendor management processes, including reporting, that are compliant with the framework and policies.

Each element of the framework is dependent on other elements. If these dependencies are not sufficiently incorporated in the vendor management program, organizations may miss significant requirements. For example, without clearly articulating performance reporting requirements, the company may adopt inadequate enabling technologies. As a result, while some organizations may elect to implement elements of the framework on a piecemeal basis, our experience suggests that to achieve the maximum value from vendor management, organizations need to implement an integrated framework across all of the elements.

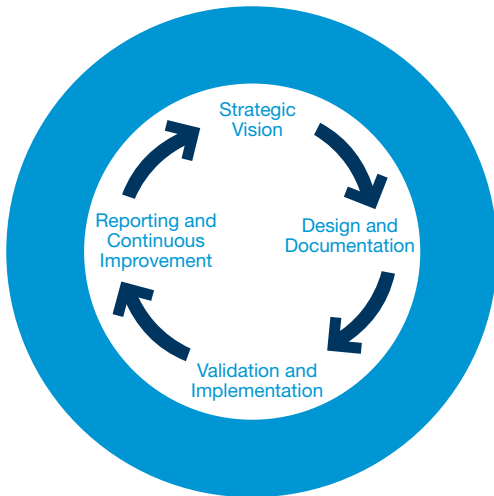
Each organization has unique requirements for the management and monitoring of vendors. The Vendor Management Framework must be tailored to the unique requirements of an organization in order to accommodate these specific needs and deliver expected results. While each organization may approach the development of the framework differently, the following steps should be performed to identify, validate and operationalize these requirements.

- 1. Develop the Strategic Vision –** Critical to the development of the framework is the strategic vision for vendor management. The vision defines the desired organization, capability and scope of vendor management activities. The vision should be created with the input of all key stakeholders (e.g. procurement, finance, legal, operations, etc).
- 2. Design and Documentation –** The strategic vision is brought to life through the design and documentation of the framework. Each of the elements of the framework will be designed and tailored based on the specific requirements defined in the strategic vision. Each of the elements is documented to facilitate the validation, roll out and ongoing execution of the framework.
- 3. Validation and Implementation –** Key stakeholders should be provided the opportunity to validate and vet the framework to confirm that their specific requirements have been addressed. Validation of the framework will support the development and

execution of roll-out plans, while creating improved awareness for vendor management.

- 4. Reporting and Continuous Improvement –** Executing the new vendor management framework usually includes making company-wide changes to accommodate the new governance processes, operational roles and responsibilities. Additional implementation activities may include change management and communications, process reengineering, progress reporting, as well as system requirements definition and selection.

An effective vendor management program, built on this framework, provides organizations with greater control and knowledge of its relationships with vendors. With this knowledge and control, organizations can apply the appropriate level of resources to each vendor and involve strategic vendors in long-term planning. Improved insight into the performance of each vendor through standardized reporting enables early identification of negative developments,



facilitates a comparison of performance between vendors and provides a vendor management dashboard for senior executives.

A properly structured and enforced Vendor Management Framework will provide measurable strategic value by:

- Formalizing practices to measure and manage vendor performance through targeted policies, controls, processes, accountabilities and governance structures;
- Enabling the organization to proactively manage and mitigate vendor specific risks;

- Clearly defining the interaction points between the vendor and the organization throughout the vendor management lifecycle to ensure consistent treatment of vendors according to their strategic or tactical value;
- Providing insight on the spend and performance of vendors;
- Reducing contract non-compliance (and associated costs and effort);
- Avoiding overpayment and/or under delivery;
- Better positioning the organization in ongoing vendor negotiations to increase value; and

Vendor risk management

Many organizations are increasing their reliance on third parties to support their business functions. While these organizations are monitoring the performance of these vendors against their contractual obligations, few are measuring and proactively managing the specific risks associated with each vendor. This places the organization at risk of a disruption in contracted services in the event that a vendor fails or experiences a debilitating event.

A critical component of vendor management is the identification

and management of risks associated with vendors. Early identification of deterioration in a vendor's condition enables an organization to develop back up plans to ensure continuation of services should the vendor fail.

Leading organizations are turning to web based tools that combine vendor corporate information, contract performance information and public information to monitor the "health" and performance of the vendor. The use of these tools enables early detection and proactive management of developments such as missed Service Level Agreements (SLAs) and contractual

commitments (e.g. the completion of a SAS 70), the deteriorating financial condition of the vendor or negative market events impacting the vendor.

In working with a number of organizations in assessing vendor risk management and/or implementing the "PwC Supplier Self Reporting Tool", PwC has observed organizations achieve the following benefits:

- Reduced reputation and regulatory risks;
- Improved controls; and
- Reduced costs.

- Engaging key vendors for input and support into long-term strategic planning.

Overall, taking a holistic approach through the use of a Vendor Management Framework can help organizations improve competitive positioning through the strategic use of vendor capabilities, reduce costs through leveraging volume discounts, build greater uniformity in the treatment of vendors, exert greater control over vendor related activities and improve vendor performance through consistent monitoring and enforcement.

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