Abstract
This paper explores and articulates the (usually) least focused but significantly important area of any organization’s spend management – known as tail spend / low-value spend management. Various factors exist behind this paradoxical situation and we investigate them right here, from defining what is tail spend, to why a firm should pay attention and make the right investment on it, while still focusing on high-spend / core areas.
What is tail spend?
Tail spend is that spend for any firm, which is not actively managed in all the spend categories and may have an impact on the firm’s financial performance due to its impact on SG&A and COGS. It contains a small portion of the spend (10–20% under each spend category) but large number of suppliers accounting for it.

We have defined tail spend in a number of ways, depending on the firm’s as-is definitions, focus areas, procurement performance, and to-be procurement maturity and performance goals. With Infosys, many organizations have defined and scoped tail spend for assessment as per the usual one, out of many definitions listed as under:

- Off-contracted spend
- Fragmented spend
- Low-value spend
- Low-value transactions
- Non-PO spend
- Commercial / one-time vendor
- Unclassified / misclassified spend
- Maverick spend

A thorough spend analysis and tail spend assessment needs to be done to arrive at the optimum definition(s). The section titled ‘Taking charge of tail spend’ details the way in which the right definition could be arrived at.

Why is tail spend management needed?
Increasing pressure on cost reduction and sustained savings through purchasing is making organizations sit up and take notice of their tail spend. From our experience, following objectives have usually been the drivers behind such initiatives taken up by several of its clients:

- **Spend coverage and savings**
  - Increase coverage of spend managed by sourcing firm
  - Improve visibility of low-value spend
  - Identify and implement opportunities for sourcing savings
  - Eliminate / reduce transactions and transaction costs
  - Reduce cost of procurement function

- **Process improvement and optimization**
  - Identify opportunities to improve process and data quality
  - Reduce business risk by increasing contract coverage and compliance
  - Eliminate trivial suppliers as and when an opportunity is presented
  - Embrace global delivery model in procurement

- **Effective management of this spend**
  - Provide end-to-end execution support to manage tail spend
  - Increase diversity of supply base (MWVDBE) quickly
  - Manage maverick spending and prevent frauds
  - Increase compliance to internal policies and external laws (eg. SOX)

Challenges faced in arriving at tail spend
The most common challenge faced by organizations while trying to segregate tail spend is ‘poor data quality’. Typically, spend data consists of incorrect suppliers and material names. Incorrect or absence of data linkages, duplication of data, presence of junk characters in the data are a few examples.

- In some organizations, lack of adequate integration between two systems such as the procurement system and the contract management system makes it difficult to arrive at the non-contracted or the off-contracted data
- Tail spend is known for its high number of sub-categories, huge item counts, and a substantially high number of suppliers. The sheer volume of ordered line items and a long list of suppliers can complicate spend analysis in spite of the low value of spend
- There are possibilities that business groups of the same firm are working in silos with decentralized policies and processes. In such cases, to consolidate the data from various operating systems requires time and substantial manual efforts

There is already a growing awareness that data cleansing and classification leads to greater spend visibility and informed decision making. However, significant analytical capabilities are needed both in the extraction and cleansing of the data and in performing the spend analytics. Not only is there a need for technology to automate significant amount of work, but also there is a compelling need to be able to understand what the technology does, how it is used, how it can be best applied by the sourcing team to cater to the requirements, and how to verify and extend the results.
Taking charge of tail spend

Typically, various organizations start with a Tail Spend Assessment Project (spanning across three to six months) where the scope is to define the tail spend, evaluate scope for opportunities and then provide business case comprising of savings, investments and operating models to outsource tail spend management. The outsourcing service provider then starts transition and implements the operations (refer the case studies in this paper). Effective tail spend management would usually require the following tasks to be conducted during the analyze-to-pay cycle.

In addition to the above, various inefficient, non-value added steps (like PO-invoice mismatch error resolution, blocked invoices resolution) must be re-engineered. Application of total quality management techniques like RCA (Root Cause Analysis), PFMEA (Process Failure Modes and Effects Analysis) and value stream mapping combined with procure-to-pay tools (eg. Ariba Buyer) exception driven workflow capabilities leads into identifying preventive controls (eg. e-Invoicing / ERS, automated returns management process). Such preventive controls can be tested and processes can be modified to become error-proof. Breakthrough spend visibility procurement applications like Infosys PWB (Procurement Work Bench) system might be considered to have spend dashboards available on demand.

Analyse
- Repeated cleansing and classification of transaction data leads to more spend visibility
- A monthly refresh of data helps getting accurate data for further analysis
- Tail spend data should be classified / filtered into opportunity areas such as price variance, spend fragmentation, spot buying, off contract etc

Sourcing
(source-to-contract)
- Usual as well as category-commodity specific sourcing levers should be used
- Some of such sourcing levers that deployed are: Contracts, rapid RFx, spend aggregation, vendor rationalization, e-market place and consortium buying

Procurement
(procure-to-pay – PTP)
- Procurement methods such as catalogues, punch-outs, P-cards and E-invoicing / ERS, fully automated 3- or 4-way match (contract-PO-invoice-payment)
- These increase the compliance and efficiency of the PTP processes as well as reduce the transaction cost
The recommended framework follows the approach of mapping all commodities on two parameters – spend and ‘supply exposure’ or ‘business risk’, defined across four quadrants – strategic security, strategic critical, tactical acquisition and tactical profit.

(Adapted from – The Kraljic Matrix by Peter Kraljic)
Using this framework, sourcing strategies can be drawn across a large number of commodities. A decision can be taken as to which quadrant commodities have to be managed first and which ones later. Also, what execution plans and strategies will suit what commodities is also defined by the matrix. For the same reason, it is a complete framework for sourcing plans and execution strategy.

Benefits of tail spend management

Various research reports (e.g., CAPS Research – reducing the transaction costs of purchasing low value goods and services, Infosys Sourcing CoE) show that the potential to reduce transactions up to 60% and transaction costs up to 40% is usually achievable in the procure to pay side. Additional sourcing savings of up to 8% is possible by deploying various usual and breakthrough levers as detailed above. Increase in customer/user satisfaction up to 20% over two to three years is an added benefit that can be easily obtained post implementation of the program.

Listed below are multiple benefits experienced by our clients:

- Positive ROI
- Reduction in maverick spend
- Increase in the percentage of contracted spend
- Standardization of processes across business units
- Increased efficiency and compliance to the procure-to-pay process
- Increase in the customer satisfaction score
- Improvement in supplier relationship management score
- Increase in SOX compliance
- Increase in MWVDBE compliance
- Reduced cost of procurement function
- Reduction of transactions
- Reduction of transaction costs
- High contract compliance
- Detection of frauds
- Strengthening of procurement controls
Case studies

Case study 1: Tail spend management for a leading US telecom company

Challenges faced by client – prior to outsourcing
- Less value of spend under management
- Low spend visibility
- Non-standard processes and low process compliance
- High off-contract spend
- Poor data quality and poor archival of existing contracts
- Lack of data linkages between systems and no-vendor hierarchy

Solution
- Tail spend defined as off-contract spend
- Tail spend of US $1.5+ billion identified out of a total indirect spend of US $30+ billion
- Increase contract coverage on high spend suppliers (spend of US $1 million and above) and moving low value spend to contracted suppliers. Supplier contracting scope ~ US $400 M spend
- Identified significant sourcing opportunity category aggregation and sourcing – US $65 million spend (over 50 strategic sourcing projects)
- Many process improvements and data cleansing opportunities have been identified as part of data analysis. Unclassified spend scope – US $900+ million
- Infosys PWB (Procurement Work Bench) implemented as single spend visibility tool across and went live with start of tail spend sourcing teams operations

Benefits delivered
- Savings – US $60+ million estimated for the first year
- Process harmonization
- Reduction in maverick spend
- Reduction in spend leakages

Case study 2: Tail spend assessment project for a global electronics giant

Scope
- Spend – Euro 6 billion (Indirect spend)
- Suppliers – 70,000 plus

Client’s business objectives
- Spend coverage and savings
- Process improvement and optimization
- Effective management of this spend

Solution
- Tail spend defined as low value spend
- Tail spend of Euro 1.1 billion identified out of a total indirect spend of ~ Euro 6 billion
- Reduce off-contract spend to leverage volumes
- Consolidate number of suppliers to negotiate better prices and simplify supplier management
- Classify unclassified spend as per UNSPSC
- In price variance scenarios: Shift purchasing to low cost supplier or negotiate better prices with existing suppliers

Business value: (opportunity size)
- About 10% price difference between contracted and non-contracted supplier prices for same item
- 10-15% savings by negotiating through reverse auctions
- Additional volume discounts possible from contracted supplier when moving non-contracted item to contract

Conclusion
Over the years, as the emphasis on cost reduction and savings is increasing, bringing the tail spend under better management should be the top priority of organizations. Outsourcing the tail spend management process to a capable service provider can be a better approach for organizations for whom internal expertise, investment, or approach to effective tail spend management is unclear. Outsourcing of tail spend is being increasingly used by organizations as an option for cost-effective management and also to direct their internal resources’ time from tactical tasks to more strategic activities.

About the author

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Deepa is responsible for creating solutions customized to client context to bring out a differentiated value proposition for Sourcing and Procurement clients. She has been instrumental in carrying out tail spend management projects for clients across various industries. Her prior experiences include working with Asian Paints Ltd. as Manager – Sourcing and was responsible for global sourcing of raw materials and with Dr. Reddy’s Laboratories Ltd. wherein she procured raw materials, which catered to their North American and European markets. Deepa has done her engineering from Punjab Technical University and has an MBA from NITIE, Mumbai. She is IPSCM certified from ITC, Geneva.
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