Why Finance Leaders Should Care About Procurement and Finance Alignment

Why Finance Leaders Need to Care About Procurement

In most companies, finance and procurement have operated separately, with the two departments working in tandem only when necessary.

This process left upper management such as Chief Financial Officers (CFOs) in the dark regarding purchases, leaving them to simply pay the bills at month-end.

Even though the finance department is responsible for all company expenditures, in many cases they have been informed about expenses after the fact, often resulting in overspending and out-of-control expenses.

What Is Procurement Responsible For?

Procurement is responsible for finding and managing the proper outside resources for a business. Selecting the right services or vendors plays an

important role in properly managing your business.

For example, in this business case, Justin is the Chief Procurement Officer or CPO for a small company that manufactures desks and tables.

In his position, Justin and his team are responsible for procuring the materials needed to manufacture the furniture including wood, glue, and decorative items.

Without someone to properly source these materials and make purchasing decisions based on budgetary considerations, the cost of goods sold would probably rise, the company's profit margin would go down, and the future of the business would be negatively impacted.

But with Justin considering budgetary constraints when procuring building materials, he can help to ensure that the company stays within its budget.

But Justin isn't only responsible for procuring materials.

He also needs to source a cleaning service that can clean the warehouse weekly, locate a hotel chain that employees can stay at when traveling for business, and find a phone plan that works best for employees and fits within the budget.

In addition, once the appropriate service or vendor has been located, Justin's team is also responsible for creating a purchase order for the products or services purchased, as well as making sure that the items purchased are received on time.

Procurement is also responsible for approving invoices on a timely basis to ensure prompt payment.

Operations or Finance?

Though many organizations maintain that procurement belongs in the operations camp, case studies have shown that the best answer to the question of where procurement lies somewhere between.

On the surface, aligning with operations makes sense, since procurement involves strategic sourcing of everything from the materials, and equipment needed to operate the business, to contract management.

But in a larger sense, the entire operations department must tie back to finance to

operate properly.

This same principle applies to the procurement department. While the responsibility of procurement is to purchase supplies and materials, it must communicate with finance regularly.

Not doing so can result in overspending, reduced cash flow, and a lower profit margin.

When procurement is brought into the finance realm, and are provided with budgetary and cash flow details, they can make more informed purchasing decisions.

Even though procurement does not directly answer to the finance department, creating better alignment between the two departments can help both.

The Impact of Procurement on Businesses

Procuring isn't just about purchasing supplies or materials. Procurement policies can also impact the following areas:

1. **Travel and entertainment:** The cost of traveling and entertainment is directly tied to procurement. Involving the procurement department in the process of determining approved hotels or preferred airlines is part of the procurement process and should be treated as such. Most smaller companies will rely on procurement to handle these transactions, though larger companies may have a separate department that can handle travel expense management.
2. **Services:** If you utilize professional services in your business, you will need to involve the procurement department. Whether it's accounting, legal, or other professional services, using the procurement department when looking to secure these services for your business is essential.
3. **The Approvals Process:** While each department is responsible for ensuring the spending limits are not exceeded, the procurement department needs to play an active role in creating these processes and helping other departments adhere to them.

Aligning Procurement With Finance

Finance and procurement working together holistically is a much better management strategy than continuing to operate separately.

In many cases, the finance department has disregarded the impact of procurement on business finances, leaving the purchasing decisions to be made by the purchasing department.

By aligning the two departments, procurement will gain a more thorough understanding of finance, while the finance department will maintain better control of the buying process, and the bottom line.

What Are the Benefits of Aligning Procurement With Finance for Your Business?

Alignment can be beneficial for both departments. These are just a few of the benefits of aligning finance and procurement.

- **Shared goals:** On the surface, finance and procurement may seem to have two very different goals. After all, the finance department is in charge of maintaining the bottom line and keeping the company profitable, while procurement is about purchasing the goods and materials needed to keep the business running. But if you look beyond the obvious, the two departments are necessary for one another, since without the materials purchased by the procurement department, the business could not be profitable.
- **Better procurement strategies:** Without guidance from the finance department, the procurement department will make its purchasing decisions independently. But with structure and guidelines in place that will need to be followed, the procurement department can make more informed decisions on the goods and materials purchased.
- **Better understanding of the finance process:** Purchasing goods and materials for the business is a tremendous responsibility. That’s why having a better understanding of company budgets, potential cost savings,

and cash flow is so important.

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Better Alignment Can Produce Better Outcomes

Finance and procurement are perhaps the two most important departments in any business, tasked with managing cash flow while also spending the appropriate amount of money to keep the business operating effectively.

While the finance department is in charge of creating budgets, tracking expenses, and creating spend management reports, it's impossible to manage spending levels without the proper guidance and input from procurement teams.

It's also impossible to properly manage risk, particularly supply chain risk if procurement and finance don't work together.

In a traditionally hands-off approach, procurement would be responsible for dealing with supply chain issues.

Unfortunately, without a good risk plan in place, millions of businesses have been left unprepared to handle unexpected product and materials shortage due to global supply chain issues.

And because the supply chain issues directly impact both business operations and profitability, it's more important than ever before that finance and procurement work together to find a solution that works.

One of the ways that business owners are dealing with procurement is by utilizing Procure-to-Pay (P2P) solutions.

The procure-to-pay process offers complete automation solutions for requisitioning goods, services, and materials that the business needs to operate efficiently.

But P2P solutions also include the accounts payable process, which is traditionally part of the finance department.

Because of this overlap, it’s more important than ever that procurement and finance teams work together.

Ideally in a P2P environment, the following would be considered procurement functions:

Suppliers

Part of procurement’s responsibility is to search for, identify, and select the suppliers that will work best for your business.

This can include everything from the wood you need to source to build custom furniture, to the hotel chain that your employees stay at during business trips. If it’s a recurring purchase, procurement should take the lead.

Setting Spending Limits

This is where it’s important that procurement and finance work together. Part of the procurement process needs to include adherence to spending limits.

It’s also vital that an approvals process be built into the procurement process.

Purchase Orders

Purchase orders are an important part of the procurement process. Purchase orders help streamline the entire ordering process from initial purchase requisition to approved purchase order.

Purchase orders also root out inefficiencies, by helping to clarify what has been ordered, and can even specify the delivery date.

Purchase orders also provide a frame of reference when it’s time for invoice processing, which is typically a finance function.

Subsequent Supplier Management

Once a supplier has completed onboarding, maintaining and managing a supplier

relationship is key.

Are your current suppliers delivering products as promised or are they frequently late?

Have they raised their prices significantly or changed payment terms unexpectedly? By properly managing your suppliers, you'll be much better equipped to handle any issues that may arise.

Ready To Make Some Changes?

When you're ready to bring finance and procurement together, take some time to do the following.

1. Identify areas where finance and procurement can work together. This could include creating a cost reduction plan, working together to identify and utilize different suppliers, and improving your current risk management plan.
2. Create a set of KPIs for your business that includes procurement and use those metrics to measure your cost savings. Your company CFO is tasked with creating a viable financial plan. But it's impossible to create an accurate plan if your CPO or procurement team is not actively involved in its creation.
3. As long as finance and procurement continue to operate independently, alignment will be impossible. Collaboration with finance and procurement, working together, makes the decision-making process that much easier, clearing the path to shared goals.
4. A lack of communication can increase errors, lead to a host of unhappy workers, and can undermine the progress of both departments. Keeping colleagues informed in real-time will be beneficial both short-term and long-term.

Business partners and stakeholders alike will appreciate the numerous ways procurement can impact your business' long-term sustainability.

Whether you're running an ERP system or standard accounting software, consider implementing a procure-to-pay solution for your business today.

What’s your goal today?

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