

# Procurement Models: An Explanation



When it comes to procurement, there are many approaches to getting the products and services your organization needs to run smoothly.

The strategy you deploy can greatly influence your bottom line and give you a competitive advantage.

That's why it's important to understand the various procurement models that are available.

Using procurement models makes it easier to understand complicated and confusing concepts within procurement.

These models make it easier to focus on your objectives and to simply communicate your strategies more effectively.

## 5 Basic Models

### Local

Under this model, all activity, decision making, and control is autonomous and

done locally.

## **Central**

With this approach, procurement activity and decision-making is centralized. There may be local activity and controls beyond the scope of procurement, for instance, calling off Supply under a centrally negotiated contract.

## **Network**

With the networked procurement model, activity is coordinated across local units. Decision-making isn't independent but remains controlled in some shape or form by various nodes on the network.

## **Federal**

The federal model is a hybrid model of the central and local models. Some categories are controlled at the local level While others are centrally controlled.

The use of the word "federal" indicates some kind of central governance.

The autonomy at the local level can be determined either by mandate or mutual agreement usually from the center.

## **Centrally-Led Network**

With this approach, activity is coordinated across all local units while control is exercised by nodes on the network. The center operates as the primary node.

# **Procurement Models According to the Next Level Purchasing Association (NLPA)**

## **The Dominick Formula™ (2006)**

With this procurement model, there is a way to score prices for comparison with a multiple criteria scorecard The formula is built on the principle that the penalty to a supplier's pricing score should be proportionate to the degree that it's price varies from the lowest qualified bid (LQB).

For instance, a criterion may be location with a maximum of 50 points.

Evaluators may award 50 points if the supplier is located within 20 miles of your plant, 25 points if the supplier is located between 20 and 40 miles away, and zero points if the supplier is located more than 40 miles away.

If a supplier's price is 25% higher than the QB, its pricing score should be 25% lower than the pricing score of the supplier submitted the LQB. If the supplier's price is 40% higher, the pricing score should be 40% lower.

The Dominick Formula is:  $PS = MP \times (1 - ((SP - LQB) / LQB))$

Where:

- PS = Pricing Score
- MP = Maximum Points
- SP = Supplier's Price
- LQB = Lowest Qualified Bid

## **The Procurement Funnel™ (2012)**

With the Procurement Funnel approach, you have a graphic representation of how various factors influence your cost savings have on your bottom line.

Procurement leaders can then focus on all the factors and metrics that can help a procurement team reach its cost savings potential.

At the top of the funnel working down, you have:

- Total Spend
- Spend Under Management
- Addressed Spend Under Management
- Negotiated Savings
- Realized Savings

## **The Dominick Matrix™ (2013)**

The Dominick Matrix is a procurement model that guides a procurement organization to choose one of four strategies for working with a supplier.

The strategy you select depends on two factors: the supplier's materiality to your business and the supplier's sophistication level.

In terms of materiality you have a range from tactical to strategic and sophistication level ranges from unsophisticated to sophisticated.

You can use one of four approaches to work with suppliers. These are:

- **Supplier Collaboration:** Working with decision-makers at a supplier to determine improvements that can have a miserable and positive financial impact for both organizations.
- **Supplier Development:** Devoting some of your resources to a project that develops your suppliers capabilities or expertise beyond their current level
- **Supplier Management:** Collecting metrics about a supplier's performance for your organization then sharing those metrics with the supplier and implementing ways that the supplier can improve its performance based on those metrics.
- **Supplier Rationalization:** Reducing the number of suppliers by consolidating purchases with fewer suppliers.
- For sophisticated strategic suppliers, use supplier collaboration.
- Use supplier development for unsophisticated yet strategic suppliers.
- When working with tactical sophisticated suppliers, use supplier management.
- And when working with unsophisticated tactical suppliers, use supplier rationalization

## **SPSM-BOK Mastery Model® (2014)**

The Strategic Procurement and Supply Management Body of Knowledge (SPSM-BOK), refers to a collection of authoritative educational materials as well as documented best practices.

These materials represent the required competencies for excellence in procurement.

The Mastery Model is a four-level roadmap to developing those competencies. It's designed to improve results from your procurement department.

Each level contains four to six competencies, each building upon the previous knowledge. The levels are as follows:

#### Level 1: Essential Procurement Skills

- Tactical Purchasing
- Analysis and Spreadsheets
- Contract Law
- Negotiation
- Purchasing Best Practices
- Sourcing

#### Level 2: Global Procurement Management

- Purchasing Management
- Project Management
- Basic Global Buying
- Advanced Global Buying

#### Level 3: Enterprise-Wide Procurement Influence

- Basic Finance
- Advanced Finance
- Inventory Management
- Supply Chain Quality

#### Level 4: External Procurement Influence

- Social Responsibility
- Supply Chain Sustainability
- Supplier Diversity
- Executive Leadership

Individuals in the procurement profession can use this to plan their career development.

Procurement leaders can use this to plan competencies they want each team member to develop.

Procurement leaders can also use this model to develop a competency-based organizational hierarchy.

# **The Continuous Strategic Supplier Evaluation Cycle™ (2015)**

This procurement model assumes that just because a supplier relationship is perfect in the beginning doesn't mean that it will remain so forever.

The continuous strategic supplier evaluation cycle begins by moving from unstructured buying to strategic sourcing to supplier relationship management. The cycle should continue with a point of supplier re-evaluation.

At this point in time, you must determine if a strategic supplier's goods or services are something you need anymore. If you find they aren't, you'll move to supplier disengagement.

If you find that the goods and services are needed then you can use a variety of questions to determine if the supplier is worth keeping which takes you back to the supplier relationship management phase or not worth keeping which leads you back to the strategic sourcing phase.

The goal with this procurement model is to ensure you have the optimal supplier for both current and future circumstances. It is up to you to determine the supplier reevaluation point and frequency.

## **Dominick's Sourcing See-Saw™ (2015)**

It's rare to come across a situation where both buyer and supplier have equal leverage in a negotiation or sourcing project.

Leverage is largely determined by the supplies market conditions. Dominic's sourcing seesaw is a procurement model that aims to help procurement professionals easily assess where the balance of power lies in any particular sourcing project.

As a buyer, when you have more leverage than a supplier, you can rely on aggressive negotiation tactics.

Threatening to purchase products or services from another supplier is an effective tactic in this situation but if the supplier has more leverage it won't work that well.

You must use different sourcing and negotiation strategies based on the current supply market conditions.

You can access those conditions with the sourcing seesaw.

Doing so helps you determine whether you as the buyer have more leverage or if the supplier has more leverage.

Questions to ask include:

- Is the availability of capable suppliers high? Medium? Low?
- Is the accessibility of pricing information high? Medium? Low?
- Is the availability of alternative products or Services high, medium, or low?
- Do you have high, medium, or low Prestige of the customer to suppliers?
- Is your organization's Financial Health high, medium, or low?
- Do you have a high, medium, or low organizational spend on the product or service?
- Is the cost for new suppliers to enter the market high, medium, or low?
- Is it difficult for a supplier to establish sales channels? How difficult is it?
- Is current growth in the market high, medium, or low?
- How cost effective is it for the buying organization to switch suppliers?
- Is the differentiation of a supplier's product or service high, medium, or low?

*To take advantage of procurement solutions designed to give your company a competitive edge, procurement functions should focus on creating value added contracts with strategic business partners.*

## **Preparing for Next-Gen Procurement**

To remain current and competitive, your procurement function has to navigate new markets and sources of supply while balancing the benefits of global sourcing and standardization against risks associated with Logistics and then need to tailor supply chains to the requirements of the local market.

It's crucial to develop and coordinate a set of capabilities that use technological advances, management, and analytics.

This next-generation procurement operating model restructures procurement's relationship with its internal customers and supply base. Interconnections between the various activities required to drive value across the entire purchase to pay cycle is critical.

## **The Right Procurement Operating Model**

Perhaps the blessing and the curse of procurement is that there is no one-size-fits-all approach. It adds to the complexity of the entire purchase to pay process, but changes in strategy are what give you the advantage over your competition.

Ultimately, your procurement operating model has to start with an understanding of your overall business strategy and align your procurement practices with those desired outcomes.

For instance, if your organization is in growth mode, your procurement strategy needs to emphasize supplier Innovation, development, and management.

If on the other hand, your organization is focusing efforts on profitability, more attention needs to be directed to traditional sourcing activities that reduce the cost of supply.

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