How to **Wipe Out** Your Costs And **Grow Stronger**

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Profit Leaks

Practical ideas to save your company thousands!

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Introduction

Supply chain and finance analysis provides a starting point for businesses and organisations that want to reduce spend and improve efficiency. If a finance or procurement manager can better understand their organisation's spend structure they can make informed decisions based on facts rather than intuition. Familiarising yourself in all aspects of the procurement process can help focus your attention on areas of your business or organisation that can be improved.

In this book we cover several aspects of the procurement process, from embezzlement culture to negotiation and provide tips along the way that will potentially help you to save thousands of dollars each year. We use our experience to delve deep into the world of procurement management and highlight the areas that finance managers and business owners must laser focus on to achieve real cost savings in their business.

In recent years it has become harder and harder to generate sales, given the continued increase in competition across most if not all industries. For small and medium sized businesses this means that managing procurement factors can be just as important when attempting to improve the bottom line.

Similarly, with globalisation, most companies and organisations can do the work they do and deliver the products that we have grown to love thanks in part to the accessibility of services, supplies and components that are purchased from outside the organisation. This has increased the importance of the procurement function.

What's more… market factors such as economic downturn and uncertainty can also increase the weight being put on procurement across all industries. The roles of procurement specialists and cost control officers have gained importance since the last global recession.

In general this book aims to provide you with ideas about how you can make your organisation much leaner in the way it does business. Each chapter is structured so that readers can gain an indication of the sums they can save in their organisation (based on company turnover) by following simple and practical tips.

We aim to help finance and procurement managers to answer three basic questions:

1. What should we buy?

2. Who should we buy it from?

3. How should we go about buying it?

The book provides readers with a holistic view of the activities that your finance department should be focussed on to achieve true efficiencies and cost control. These activities include everything from basic accounting activities to sourcing, purchasing, negotiation and fraud awareness.

In short, by managing these procurement factors, organisations can control their spending and reduce risk in their business.

The industry insights and real-life case studies contained within this book are based on our experience having spent a combined 20 years in the procurement and finance industry. Our roots lie in providing small to medium sized organisations with a revolutionary software product which enables them to control and reduce costs related to procurement.

One of the most powerful lessons we have learnt in recent years is that organisations can only implement successful cost control and spend management initiatives by aligning these efforts with their overall business strategy.

Half hearted procurement management initiatives simply fall by the wayside if a full commitment is not given from everyone at management level.

Read this book if you want to:

- Improve your companies bottom line by focussing solely on procurement factors.

- Reduce end product costs.

- Keep working with and find forward thinking and innovative suppliers.

- Get better at identifying sourcing opportunities.

- Get a better understanding of the metrics that drive improved cost efficiency.

- Get a better end-to-end view on your company spending.

Accounting

In the early noughties I was working for a large Irish multinational. The company was a leader in the baked goods production. In fact the company was responsible for the creation of the chilled baked goods industry. Each day we supplied thousands of chilled baked goods to store around Ireland. The management and staff at this company therefore were highly skilled, knowledgeable and experienced. This was a business at the top of its game, with highly paid and trained managers...what could go wrong.

At this time the business was heavily involved in acquisitions and mergers. They surveyed the business landscape for opportunities to acquire companies in the baked goods industry which they could buy and add value, thus increasing the overall market value of both companies. During this time a company appeared on the radar. It was a baked goods company based in Wales, UK. The business made local treats such as baked "faggots". Faggots are meatballs made from minced off-cuts and offal, especially pork (traditionally pig's heart, liver, and fatty belly meat or bacon) together with herbs for flavouring and sometimes added bread crumbs. It is a traditional dish in the United Kingdom, especially South and Mid Wales and the English Midlands.

The Merger and Acquisitions team were immediately despatched to run the rule over the business. This involved detailed analysis of the revenue, cost of sales, gross profit and overheads. The managers needed to be sure that everything could backed up before any detailed discussion on an acquisition could commence. Once this was completed the offer was made and accepted for the business. Now the real work could begin.

Part of the business tactics was to always send in a locally homegrown trained accountant to take over the finances. This is an idea stolen from Kerry Foods. Kerry Foods have large number of businesses outside of Ireland. To make sure they can always keep a close eye on them they would hire an accountant in the country / region where they had the business. Next they would bring the new employee to County Kerry for a 12 to 18 months to train them in the "Kerry Way". This meant they got indoctrinated in the thinking, culture and work ethics of the Kerry Group. Once complete the new accountant would be despatched back to the foreign business. This was a great way to operate for many reasons but three stand out;

- The new employee for the start had allegiance staff at the Kerry Food head office

- They were changing the finance department in the acquired business but not the manager or operations, so what had made the business successful in the first place did not change

- Finance is typically where all the bodies are buried. If you have a strong accountant then you have complete knowledge of the business. There are no surprises.

The accountant selected for this job was a friend and colleague of mine. We had worked closely together when I first started at the group. I liked and admired this person who worked long hours and knew his stuff. So off he went to the new UK acquired business. Initially all seemed to go well. He reported numbers each month and they were just less than budget, so nothing there to warrant any further investigation. The real issues began when a second accountant was sent over to help him. This accountant had also been trained by the local Irish team. He had worked in payroll for quite a while but now wanted to get some experience in the other areas of the finance department. The numbers were reported as normal the next month and I knew immediately that there was something up. The senior managers in the Irish business all disappeared for a few days. To me it was clear there had been a major issue in the UK business and they had gone over to investigate. Little did I know that the issue was in the accounts and directly affected the two accountants whom I had previously worked with in Ireland.

Once the managers came back the truth slowly began to emerge, but I got the inside line direct from my colleague who had arrived back in the office. Over a coffee he told me the sorry but all too common tale. When he arrived he had trusted that a business that long in existence would have bullet proof procedures. Sure they may have had outdated IT systems and things could be slow to get done but he was confident that they would have ways to track and understand their business to compensate for these shortcomings, but he was very wrong. He began reporting the numbers as he had been thought more or less on budget. The budget after all is derived from last years figures so it usually not too far out. The issues surfaced once they began receiving invoices for which they had no accruals, purchase orders or goods received notes. Were these invoices sent to the incorrect company or already posted. Checking with the supplier it turned out the product, in this case truckloads of flour had been delivered. This could mean only one thing, they had not accounted for several loads of flour, which meant they had missed out of thousands of pounds of costs each month. Suddenly the figures went from nearly hitting budget each month to a massive loss. This as you would expect had serious consequences for this career.

Chapter Summary

Purchasing and procurement managers need to remember that accounting matters.

In the next ten points we cover issues that need to be kept in mind when you are thinking about accounting and procurement.

Mistake #1: PPV

Purchase price variance is a key metric that should be tracked by most businesses. It is the difference between the price you agreed to purchase a product or service and the actual cost. It is mainly used in manufacturing companies but should be used more widely as it can give great insights into where a business is losing profits.

An example of PPV is as follows;

John goes to order 5,000 pieces of component A. The system is set up for standard costing and so holds a cost for this component of $5. When John goes to the supplier to purchase a new batch of these items the price is now $5.50 per piece. This gives the company a

PPV of $0.50 per piece or $250 for that one order.

Of course the PPV could have gone the other way and they could have made a saving if the price had decreased and was lower than the standard cost.

Some of the benefits in monitoring the PPV include they can tell you if you are losing money on items due to buying decisions, they can help you monitor the purchasing team performance and they can help direct innovation as you should look to substitute items that are increasing in cost.

Mistake #2: Approval Matrix

This is a list of people who can sign off on different levels of spend. Setting up an approval matrix is one of the first actions you should take if there is not one already in place.

An approval matrix benefits include:

- Insuring the company does not commit to spend that is not recoverable.
- Controlling spend.
- Making managers aware of committed spend.
- Excellent audit trail.
- Ensures compliance with anti fraud

When setting up the matrix you need to take into account who are the decision makers in the company. Also important to understand the culture. Putting in these types of controls can be a shock to the system. There will be a lot of push back from managers and employees who are used to just buying what they want when they want, but it is key to persist as the benefits are substantial and ongoing.

Implementing something like this can be made easier using software such as that provided by https://www.procurementexpress.com. This can take the hard work out of setting up the new processes and procedures but also the ongoing maintenance which can be very time consuming if not managed correctly.

Mistake #3: Copy invoices

In the world of digital documentation it is now all too easy to receive the same invoices twice if not thrice. This can cause havoc if you have not got the correct systems and procedures in place. Even with the correct system up and running it can still be overruled. Never underestimate the power of people to make a mess of something.

I personally have seen the following examples:

- System, correctly I might add, won't accept the same invoice number from a supplier as it is already posted, so the accounts payable person adds a "1" to the last digit.

- They might see an invoice amount already there that is similar so they just post it to another account.

- Two invoices, different amounts but the same invoice number, the larger once can just get posted instead of investigating the issue.

Mistake #4: Fake Invoices

While posting onto the system and paying an invoice twice can be troublesome, paying a fake invoice has more serious consequences. Paying a current supplier twice, when you have picked it up doing a supplier reconciliation, just means that you need to contact them and agree to reduce the overpayment off the next payment run. If you end up paying a fake invoice issue is that you cannot get the money back and you still owe the original supplier.

Greater still is the risk that you do not pick up that this supplier was fake and continue paying their invoices, which they of course will be more than glad to keep sending you. This can lead to a vicious circle of incorrect reaffirmation were because the supplier was paid previously they get paid again, etc.

In most cases these fake invoices create real costs that should be picked up by the accountant, but you can never be too careful. At the end of this section we detail best practice to keep your business safe.

Mistake #5: Lack Policies and Procedures

I know of a company were a manger would just walk into accounts, pull out a scrap of paper with some bank details on it and ask for $X,XXX amount to be transferred to the account details thereon. This was blatant fraud but it went on for years costing the company hundreds of thousands of euros. How could this happen, well the person was in a position of trust for a long time, their accountant was asleep on the job but the real reason was a lack of policies and procedures.

Policies are overarching guiding principles. They do not go into specific details but are more a way to think about how things should be done. So for a purchasing department a policy might be that nothing is ordered unless it has a valid purchase order or that the approval matrix is used for all purchases.

Procedures go into the detail on how the policy is implemented on a day to day basis. So for the example of approval matrix used for all purchases the procedure could be as follows:

- Ops make a request for purchase of product / service on the purchase order system.
- Based on the value the System uses the approval matrix to decide who needs to approve this potential spend.
- An email is sent to the appropriate approvers asking them to approve the spend.
- Once approved by the relevant people a purchase order number is generated.

- The PO number to emailed to the requestor who can then send onto the supplier.

In the end the company in my real life study called in the police. The person went to jail but could not repay any of the stolen loot. The accountant who did not spot the issue did not get fired because he was a personal pal of the CEO. Good to have friends in high places.

Mistake #6: Accrual Principle

This is to match your income to your costs.

The second main function of a good purchase order system is to allow the accountant accrual the right amount of cost into the monthly management accounts. Without accurate accruals the reported numbers are effectively meaningless.

Monthly management accounts in small businesses are important but they are not the be all and end all as the owner / manager is usually close to the daily going ons and already knows what the numbers will be for the month, quarter or year. Where they become super important is in the medium, large and multinational companies were the accounts can affect the share price, banking facilities and worse of all effect bonuses. It is here that we need to see the implementation of software to drive best practice which will enable the team of accountants to report accurate numbers in the period.

When this goes wrong we only need to look at scandals at companies like Tesco and Enron to see the complex way that accounts can be used to mislead as well as inform. At Tesco UK they decided to boost their profits by taking in a large amount of supplier income. Yes, you read that right, income from suppliers. In the trade this is called retailer contribution. The supplier pays money to the retailer. Why? Many reasons, including: to get stock on their shelves, to get end of shelf product placement, to get promoted within the store. It used to be that retailers made money from buying a product at $1 and selling it for $1.50, but that has changed. They now make a considerable amount of their income from RC. Hard as it is to believe the suppliers are now paying the retailers.

How does this tie back to accrual principle. Well Tesco got under so much pressure to report amazing figures that they started taking in RC that had yet to be received or even agreed. The income didn't fall cleanly under any accounting standards so Tesco argued for years that this income should be included. This worked up until 2014 when it seems the game was up and the auditors pulled the plug on the whole sorry mess. The result was a massive scandal, hundreds of millions in fines, careers ended and share price collapse. Who says accruals don't matter.

Mistake #7: Fake Emails

This, along with social media is the scourge of the modern age. Millions of fake emails are sent into accounts departments the world over. The range from the ludicrous emails from next of kin of Afirican dictators to the sophisticated emails from your boss.

Boss emails include the following types:

In a meeting

I'm in a meeting, can't take any phone calls, but I need to get a transfer made today. Once you reply they will give you more details and ask that you actually make the transfer.

Are you in the office?

Sometimes the email chain can start off with a simple question. Their goal here is to get you to reply so that they can start an interaction. You will also trust their email address and it will start appearing as a default in your Outlook address suggestion list. Really it is about building trust so that they can move you onto the next stage which is the making of payments.

Let's make the payment

Finally as a period of time once trust has been gained and you believe you are really emailing with the CEO they will ask for the payment. At this stage they will include full account name, bank details and the amount to be transferred. Needless to say that if you make this payment you will never see the cash again.

On the other side we have the weird and wonderful spam emails. One of the more bizarre examples arrived in Ireland in 2012 as follows:

> *As I sit here sipping a martini it is my regretful duty to inform you that you have been selected for assassination.*
>
> *I am a professional assassin (I enclose my certificate of assassination as proof) and SMERSH have contracted me to assassinate you and have specifically paid extra for a particularly nasty death which makes it look like you died in a particularly bizarre sex game gone wrong; I had already bought the shire horse stallion (he's called Henry – picture attached), the lard and the dragon dildo (from Bad Dragon of course, I only use the very best tools) when I found out that you are innocent of the accuse, so I make out this time to contact you. Unfortunately international crime syndicates won't admit to mistakes and cancel the hit so I will be forced to carry out the assassination on you. Sorry about that old chap but rules are rules.*
>
> *There is an option for me to help you in other for you to know who had paid SMERSH for your DEATH and don't forget my men had been monitoring you for the past few days and daily record of your activities is been sent to me but I have refuse to order your DEATH.*
>
> *Get back to me if you value your LIFE with all due speed or else I regret I will have to carry out my original contract to assassinate you and although he is quite charming for a horse I don't think Henry is the most sensitive of lovers.*
>
> *Toodle Pip!*
> *Dai Teatime*
> *International Assassin*

Although anyone reading this was probably alarmed at the time things have moved on since 2012 and most sensible people would just ignore this kind of threat.

Mistake #8:Stock Control

In the history of lost profits missing never has so much been lost by so few then in the dark and mysterious world of stock control. Sure there are companies that operate Just In Time purchasing, DELL computers being an excellent example, but the reality is that most same and medium sized businesses are losing stock at sometimes alarming rates.

Issues for stock are legion:

- Obsolescence
- Damage
- Over buying
- Wrong stock
- Misplacing Stock

Where to start. The issues here can devastate a business. A simple example of over buying leads to too much working capital, too much cash tied up in stock and then to insolvency. This would never happen to us I hear you cry, but I bet any business operating in Ireland and the UK have stockpiled for the mythical Brexit and are now having to get rid of stock as fast as they can to pay off their suppliers.

Mistake #9: Errors

Sometimes the little details can have a big impact. Once I worked for a business that was involved in construction. Now construction has a strange tax called RCT (Relevant Contract Tax) which means that if I am the principal contractor on a project and you are a sub contractor working for me them I take RCT off any payments I make to you and pay them across to revenue. This means I have to be super careful with my records. Unfortunately, my colleague was not so careful with his spreadsheets. Instead of putting in a deduction of 20% he put in a deduction of 2%. This detail across many sub contractors meant that we were short 18% on €1.4million which is €252,000 which is a lot of money. There was no way around it and we had to pay it across to the Revenue and then claim it back by reducing payments to the subbies for the rest of the project. It was a tough lesson for all of us but particularly for my colleague.

The top tips to avoid this kind of spreadsheet error is to always sense check the numbers. Do they make sense at a top level. No need to go into the detail line by line just look at the headline numbers, is 2% of €1.4m = €28,000? Seems a bit low doesn't it. Time to get the calculator out and double check a few more lines.

Another tip is to give it to someone else to review. This can be very effective, as the saying goes when you are looking at the trees you miss the wood. A colleague or your manager having a look at the numbers when they are unfamiliar with what you are doing will mean they ask the obvious questions. Where did that percentage come from, are you sure its 2%, what did we deduct last time? All simple queries but so hard to see when you are buried in hours and hours of spreadsheet work.

Mistake #10: Balance Sheet Reconciliation

Hitler once said ""He alone, who owns the youth, gains the future." and the same could be said of the Balance Sheet in a company. While there is a lot of focus on the profit and loss account the real issues can occur in the balance sheet.

Issues that can really make it a bad day for your business include:

- Not reconciling balance sheet each period.
- Bank accounts that are not reconciled.
- Incorrect depreciation policy.
- Miscalculation of foreign exchange gains or losses.

If you do not keep a close eye on the balance sheet you can easily get hit with a nasty surprise fitting into one of the errors above. There are no excludes for not reconciling each period. Not keeping a close eye can cause you a massive amount of profit.

Imagine you are paying a supplier an upfront 25% fee for a large project. As the full cost of the project is still unknown you just pay the money as a deposit without posting any invoice onto the system. So you have to post this into your accounts at the end of the period and one of your finance team does the following journal, the credit the bank account to show that the money has gone out and they debit (remember your accounting at school; debit / credits) what? Well as you have no invoice and you do not want to show a debit on your supplier account which would effectively say that the supplier owes you money, very unusual. And you do not want to post it to the profit and loss and it will give a large loss in the month, which is incorrect as it should be capitalised. So you post the payment to another balance sheet account, maybe “Clearing” or the infamous “Suspense”. All looks good. Bank reconciled everyone’s a winner.

Six months later.

In comes the CEO. He holds an invoice in his hand for the complete project cost. Right he bellows the supplier has done the project and we are happy to pay this invoice, but no more. Supplier has said they are cost overruns but that is his problem. He hands you over the piece of paper and asks you to them them asap. The thinking being that cash in hand will placate them for the time being. You post the invoice to their account, check the balance (its the full invoice amount) and setup the payment. Job done. Except you have forgotten about that 25% deposit that was paid up front. It’s got lost on the balance sheet. You haven’t been keeping up to date with the reconciliation and now it will cost you your job.

Other cardinal sins in balance sheet recs are not keeping your bank accounts up to date. Not having a good idea of your cash position is a recipe for trouble. In fact it can cost you thousands or even your business reputation as you end up having to take short term high interest loans and also regnange on payments to suppliers who will then charge you a premium in the future as you are now deemed unreliable.

If your business is engaged in large foreign currency transactions then you need to think about currency options, swaps and futures. These can all be used to lower risk and lower cost.

Options give you the right, but critically not the obligation to buy or sell currency by a certain date. It can be valuable if you are waiting to make a call on a deal but have not yet committed. You think that the currency might move against you so you want to hedge against this risk.

Swaps work by a bank setting up an agreement between two of their client. So you might have a company A who wants to sell dollars for euros and company B who wants to borrow dollars and sell euros. For a swap to work each of these companies must be able to get the currency at a better cost than the other company. So in this example Company A has access to long term dollars at a low rate, while Company B has a surplus of euros which are not making much money on deposit. For a fee the bank will then setup an agreement where both can benefit from the others competitive advantage.

Forward Rates are a contract with a bank covering a specific amount of foreign currency (FX) at an exchange rate agreed now. Advantages include that they are simple, low up front costs, available in many currencies and available for more than one year ahead. Disadvantages include that they have a fixed date and the rate may be unattractive.

Other risks include

- ***Translation risk***: Value of overseas assets falls as they translated into domestic currency at year end or the value of overseas liabilities rises.
- ***Economic risk***: Long-term movements in the exchange rate damage the value of a company.
- ***Transaction risk:*** Value of cash flows are higher or lower than expected because of movements in the spot rate between agreement/contract and the settlement in cash.

Accounting Checklist

1. PPV

Who monitors the purchases and compares them to the PO's?

Setup a monthly report so that the variances can be reviewed..

Review the report with the managers to give them feedback.

Make changes to the purchasing as required.

2. Approval Matrix

Set up an approval matrix based on the company structure and purchasing values.

Review the matrix annually.

Make sure the matrix is followed by checking the purchase order sign off. Random selection should do it.

Using software to manage the POs is preferable. The cost will be offset by the savings.

3. Duplicates Documents

Make sure to have a robust PO system in place.

Process only valid invoices i.e. have correct VAT, PO number etc.

Make sure system will not accept duplicate invoice numbers from the same supplier.

4. Fake Invoices

Check all details on the invoice.

Does it have a valid PO number which has not been previously used.

Compare the invoice to other invoices from the same supplier.

Is the invoice for an unusually large amount.

Where did the invoice come from?

Is the format correct?

Are there spelling mistakes?

5. Lack Policies and Procedures

Develop and implement strong procedures with the purchasing department including:

Sign off before order.

Different levels of sign off based on values.

First time suppliers are checked by senior supervisor.

6. Accrual Principle

Hire a good accountant.

Understand that having costs and revenue aligned is critical to business success.

Spend time each month understanding variances.

7. Fake Emails

Keep you virus software up to date.

Immediately notify your IT person if anything suspicious arrives.

8. Stock Control

Secure your stock.

Limit access to stock.

Have weekly cycle count of the most valuable stock and the stock that have high turn over.

9. Errors

Review variances for errors.

Any errors need to be traced back to the source through root cause analysis.

Feedback given to the employees that have caused the errors.

10. Balance Sheet Reconciliation

Make sure that your accountant is doing this monthly.

Get them to follow up any issues and resolve before the next month end.

Embezzlement

Let's get things started with a story. A few years back, we counted a local high street cafe as a client. We helped install their EOPS system and every now and then would be called on to add an update or security patch in return for free coffee.

It felt like a pretty sweet deal at the time. They were based only a short walk from our offices and we got to know the staff well... as we were always back and forth in search of a caffeine fix!

The manager was an incredibly bubbly woman by the name of Vanessa. Every day Vanessa would be up at dawn rolling up the shutters, taking deliveries from the bakery and at 6am sharp she was ready to warmly welcome her dreary eyes customers. She was a hard worker and the cafe owners placed huge trust in her.

Vanessa was also a real people person and she made everyone feel good about themselves. She was really looking forward to going on a long holiday back to China where her mother lived. Vanessa told me that she hadn't been home in years and hadn't taken a holiday since moving to the city three years ago.

Finally, it was time for Vanessa to embark on her big adventure and we wished her the very best, telling her we were looking forward to seeing her holiday snaps on her return. Weeks passed and it became clear that Vanessa was not returning to her job. I began to get worried for Vanessa as the owners of the cafe were suddenly back at the helm... and handing me my coffee every morning.

When I asked them about what had happened, it was clear that I had struck a nerve. It turns out that sales in the cafe jumped by over $500 the week after Vanessa went on holidays. The same happened the next week, and the week after... until the owners began to realise that sales hadn't jumped at all. Finally, the usually absent owners were getting a true view of how their business was really performing!

Vanessa, while being an incredibly hard and diligent worker, was pocketing the cash from every couple of sales instead of depositing the money into the cash register, and essentially ripping the owners off. Needless to say, Vanessa was confronted with an ultimatum when she returned to work and was never seen in a coffee shop in our small city again. Luckily, the owners of the coffee shop were involved enough in the business to spot this discrepancy and put an end to what was a lengthy case of fraud and embezzlement that spanned years.

Chapter Summary

In this section we will be exploring the many different ways that companies and organisations can be taken advantage of by their very own staff and employees.

There are many types of embezzlement out there, and the specific nature of the fraud will usually depend on the industry that the employee works in.

This guide should go a long way towards helping you as a business or financial manager to identify embezzlement that may be happening in your very own organisation.

Mistake #1: Not being able to identify embezzlement

Embezzlement is a very particular type of fraud that's sometimes incredibly hard to prove and identify. For embezzlement to occur, the following four factors must generally be present:

- A professional connection must have existed between the two parties. This could be an employee-employer relationship for instance.
- The alleged embezzler must have taken the asset(s) or item(s) through the said relationship that existed.
- The alleged embezzler must have formally taken ownership of the asset(s) in question or at the very least intentionally transferred the ownership of the asset to someone else.

- The alleged embezzler's actions must have been intentional. In some cases an embezzler may not realise that what they are doing is actually wrong.

When analysing and approaching embezzlement we must also consider the following factors that results in an employee engaging in embezzlement.

The employee must first be presented with the opportunity to embezzle. If the opportunity to embezzle is there, there is also likely to be some external force or pressure that results in them making the choice to defraud. Lastly, the employee will often rationalise their strange behaviour. After all, the fact that the employee is in gainful employment and owes a debt of gratitude to their employer makes embezzlement a particularly strange phenomenon.

Opportunity: Embezzlement usually occurs after an employee identifies an opportunity to take advantage of the trust their employer has in them. Similarly, it can occur when an employee spots a flaw or weakness in an internal system or business process. Many embezzlers find themselves in a unique position of power in the course of doing their routine tasks. It may surprise people how many chances one has to steal money or assets when they perform a job or task over and over again. An expert in any field will always find weaknesses in a system or process - and the million dollar question is whether they take advantage of these weaknesses or not.

This could be as simple as a shop cashier finding that no-one notices when they unintentionally give a customer the wrong change. As they become more and more disenchanted with their job they may begin to repeat this apparently innocent activity and make a habit of keeping the remainder of the change for themselves.

Pressure: Most employees only find themselves in a situation where they are embezzling because they are under huge pressure of some sort. We must consider what pushes an employee that has the same working conditions, responsibilities and salary as their counterparts to put their employment and reputation on the line and actually start knowingly stealing from an employer.

Many of the employees that steal or commit a fraudulent act against their employer may have fallen on hard times, have deep rooted psychological pressures in their life or may be going through some sort of trauma or need money to satisfy an addiction of some sort.

Rationalising the Action: An employee that embezzles knows very well that they are committing a crime and in most cases they will tell themselves that their behaviour is warranted given the situation or life stage that they might find themselves in. After all, it is much easier to take what is not yours to take, when it is for something worthwhile.... or when the money is badly needed. Employees will sometimes build a false sense or perception of their employer and justify their actions by telling themselves that their employer is wasteful or has so much money that what they are doing is actually trivial.

Mistake #2: Falling victim to payroll theft.

Ask yourself how safe your payroll is.

The reality is that this depends on the people that manage and control it!

Payroll fraud involves the payroll administrator fraudulently inflating their salary or another employee's salary for financial gain that amounts to stealing. In some high profile cases payroll administrators have been known to add false employees to the payroll and collect wages for this "ghost" employee using a second bank account of their own. This is a practice that likely occurs in thousands of businesses across the country to this very day and companies are reporting a huge increase in payroll fraud in recent years.

While the above example usually relates to employees on a fixed salary, contract employees and workers who are paid an hourly or day rate can also abuse the system and embezzle funds or value from their employer by misappropriating payroll records. Workers with unclear objectives can alter the number of hours they actually work by submitting fraudulent timesheets or by getting a colleague to clock them in for work when they are not actually at work or working.

Even workers who are paid on a commission basis may be tempted to exaggerate the number of pieces they have actually sold or produced.

It's worth also remembering that companies who outsource their payroll can also fall victim to payroll fraud.

A tax consultant based in Kent and a former Inland Revenue employee stole nearly £6.9m from the wages of his client's workers. Through a complicated network of companies he, along with a number of other associates, siphoned a small amount of money disguised as a tax from each of the workers payslips.

After several of the companies he worked for became aware of discrepancies, Mike fled to countries that do not have an extradition treaty with the UK. On his return to the UK in 2018 he was arrested at Heathrow Airport and subsequently jailed for 9.5 years.

While this case demonstrates that former officials and professionals can just as easily embezzle money and commit fraud, it also demonstrates the fact that payroll fraud is usually driven by greed. Payroll fraud involves an abuse of trust and the manipulation of systems that are designed to ensure workers are paid correctly.

The success of payroll or overtime fraud will very much so depends on the level of supervision afforded to employees and the safeguards that an employer has in place to protect itself against such occurrences.

Most of our clients find that by centralising outgoing payroll and other critical accounting functions, the opportunity to embezzle is greatly reduced. By following this more closely supervised financial model there is less opportunity for theft to occur.

It's also worth watching out for early warning signs when it comes to payroll theft. Any employee who is engaging in payroll theft is likely going to be incredibly guarded and secretive. They may be unwilling to share duties or working long hours in an effort to hide their fraud. A good rule of thumb is to remember that if something doesn't seem right, it probably isn't.

Mistake #3: Missing out on tell tale embezzlement signs.

Detecting embezzlement in your organisation is easier than you might think, if you know where to look and what to look for!

By building in a number of checks into your monthly or bi-monthly risk management processes you can spot tell-tale embezzlement signs and do your business or organisation a huge favour in the long-run.

Here are a few things you should be looking out for:

1. **Watch your profits.**

Profits rise and fall in every business - however any unusual or downward profit trend should always be attributed to a stimulus. By attributing dips in profits to trading conditions or for instance to a large capital outlay - you can better understand where your companies money is going and how it is being spent.

2. **Records Management.**

If your employees are not recording all transactions, from petty cash expenditure to payroll costs, your company is at a high risk of being embezzled. Systematic record keeping is the cornerstone of a viable and sustainable business. If your records are not clear it either means that someone is cooking the books or not before long someone will take advantage of the situation that you have created!

3. **Customer Accounts that just don't look right:**

Most embezzlers transfer small but frequent sums of money out of a company in an effort to avoid detection. A common fraud involves the embezzler setting up a customer account that's connected to their bank account under a false name. The filtering options in modern day accounting systems and software can thankfully help us to detect these underhand activities easily. By regularly running reports that identify customers that were given large or multiple refunds you'll remain one step ahead at all times.

4. **Employees that work late and don't go on long holidays.**

Embezzlers often become paranoid over time. Embezzlement can easily go out of control and what often happens is the embezzler realises that their fraud will be spotted if they step away from their role for a substantial period of time.

The result is an employee who is very protective of their work to the point where the resist taking holidays in large blocks. As the fraud spirals out of control the embezzler needs more and more time to cover their tracks which results in them constantly working after hours - even during seasonal periods when workload is reduced.

5. **Employee splurges**

If you notice an employee flashing their cash around the office or a drastic change in the spending habits of one of your staff - you may have a problem.

Typically, business owners and finance managers identify embezzlers in this way - when one of their employees purchases a motor vehicle that would typically be very difficult for them to finance based on their salary.

6. **Petty Cash going missing**

It's important to remember that all losses of cash are serious - even when the amount that has gone missing is small. For many employees there is a temptation to look at the petty cash reserve as a free for all private lending source.

Managers should regularly spot check petty cash boxes and actually examine the receipts to ensure they are genuine, instead of merely glancing at them. When it comes to petty cash - every dollar counts!

Mistake #4: Believing that embezzlement is rare.

One thing that has become increasingly clear to us in the line of business that we are in is that embezzlement is incredibly common and comes in various shapes and sizes.

When people think of embezzlement they often think of brazen fat cats in their offices engaging in serious white collar crime - but in reality most embezzlement is carried out by unassuming staff members who go to extreme lengths to hide their big secret.

Smaller businesses in particular should be wary of the threat embezzlement poses to their business for the very reason that most cases of embezzlement occur in small businesses.

The main reason for this lies in the fact that small businesses often don't have the necessary checks or protections in place to deter and discourage employee theft.

It's much easier to take advantage of weak systems that lack the need for verification or accountability. In small businesses practically all employees have access to confidential information, stock and in some cases bank accounts.

Employers too often place so much trust in their employees that they forget that their employees are only human - facing societal struggles whilst trying to support their family and pay their rent at the end of the month.

For some employees who find themselves under huge financial pressure, dipping into company reserves may seem like their only means of survival.

For this reason, embezzlement of even a small scale must be taken seriously in every business. Employers that educate staff about embezzlement are the employers that people with embezzlement tendencies fear the most.

If an embezzler is aware that the company is tuned in and active in detecting embezzlement it's unlikely that they will embezzle - as they know that there is a higher chance of them getting caught.

No-one is suggesting that business owners must rule with an iron fist - that just sucks productivity - but they should remove risk by making it incredibly difficult for employees to embezzle without consequence.

Examples of how this can work included ensuring that all payments are verified and approved by more than one person and ensuring that employees no client account are managed solely by one member of staff.

Mistake #5. Not educating your staff about embezzlement.

These days, employee education is crucial when it comes to fighting embezzlement. Many employers are encouraging their employees to provide anonymous tip-offs relating to embezzlement and fraud within their department or office.

It's important to remember however that peer to peer relationships and reputation remains incredibly important in any organisational department - whether embezzlement occurs or not. Anyone that wants to remain eligible for promotions in the future and enjoy a happy working environment will be very wary about whistleblowing. Whether whistleblowing is the right thing to do or not, no-one wants to get a reputation for landing others in trouble.

For that reason it's very important to educate staff about the impact that embezzlement can have on the future of their company and their jobs - whilst rolling out a system which allows tips to be passed on to management totally anonymously.

Companies that instill a culture of "doing the right thing" and companies that invest in whistleblowing systems that guarantee employees their anonymity - can increase embezzlement detection by a remarkable factor. While 3rd party whistleblowing systems might be expensive or at the very least a hassle to establish, they actually can work and help save money in the long run.

Once a company educates staff about embezzlement they are in a position to actively encourage staff to watch each other and report any discrepancies or suspicious activity they encounter without guilt or reservation.

The issue with encouraging whistleblowing is that a feeling of distrust can develop - where employees might feel they are being unfairly watched. Everything comes down to how the system is deployed and managed in the long term. To ensure accountability and transparency, it is important to have a mechanism that enables all individuals to voice concerns internally in a responsible and effective manner when they discover information which they believe shows serious malpractice. Companies with a whistleblowing policy provide a method of properly addressing bona fide concerns that staff in an organisation might have.

Virtually any entity that implements a whistleblowing system (either by telephone, email or web-portal) will see lower losses and shorter detection times to stop the losses and catch the perpetrators. Many of our clients who encourage whistleblowing in their business report that they would likely never have discovered many of their losses without someone reporting these occurrences.

All reporting systems should have the following characteristics:

- Have the ability to identify major risks versus minor risks
- Tips offs sent by mail or unsecure email should never be encouraged as there is a risk that the information may not arrive with the intended recipient.
- Consider whether you should also accept tips from external parties
- Any reporting system must maintain the anonymity of the person making the report
- Employee education is vital when encouraging whistleblowing. Employees must understand what embezzlement is and looks like. The last thing you want is a glut of incoming false allegations.
- Before implementing a system, as an employer you have a responsibility to help understand what behaviour is acceptable and not acceptable.
- To implement such a policy the company must encourage

a zero tolerance approach. Exceptions can't be made for certain people such as senior management. Every accusation must be investigated in the same way with the same level of resources.

Organizations that use a whistleblowing system demonstrate to their employees that the threat of embezzlement is on their radar and this in itself is a sufficient fraud deterrent for many employees.

Mistake #6. Not building background checks into your hiring process.

In 2018, the Association of Certified Fraud Examiners (ACFE) carried out a major embezzlement related study and went on to find that the typical organisation loses 5 percent of its annual revenue to fraud each year.

Many companies forget that the first steps toward preventing embezzlement and fraud starts at the talent acquisition stage. Employers who invest in the recruitment process and take the time to screen and qualify job applicants will naturally have a better and well rounded pool of recruits to choose from. While vetting new recruits can be expensive, in the long-run it makes sense financially to commission background checks given the devastation and destruction that a rogue embezzler can cause.

Background checks should apply to employees of all grades, considering that even the most lowly paid workers can still potentially embezzle thousands of dollars from a company in a matter of days. Many HR and pre-employment consultancy companies offer a comprehensive range of screening services. For employers this means that they can make sure that each individual who qualifies for an interview or position is exactly who they claim to be.

Hiring a dishonest staff member can cost a company tens of thousands of dollars in the long-run, may impact staff morale and result in legal expenses down the line. Typically employers and human resources managers want to make sure that applicants are telling them the truth on their job application.

Here are a few things to watch out for when performing a background check on a new-hire:

1. **Detect false information.**

For most employers it's vitally important to check that applicants are not lying about their work history on their CV. If a person who is in the running for a job lies about their work history they're probably hiding something.

Trust must be earned over time. When a new recruit starts in a role they must build the trust of their managers and their peers by carrying out their day to day tasks diligently while treating clients and customers with respect.

It is estimated that over 90% of CVs include misleading information, and while most human resource managers expect to find white lies on CV's when it comes to past achievements, spotting gap in employment which has been disguised or masked could be enough to prove that an applicant was sacked from a previous role due to embezzlement or fraud. Examining gaps in an applicant's work history can help determine whether the applicant poses a true risk.

2. **Convictions:**

All business owners need to verify that job applicants do not have convictions for fraud that prove that they may be a threat to the business or the business's cash reserves. It may seem obvious, but new hires with a fraud conviction are much more likely than those without a conviction to stealing cash and inventory.

Mistake #7. Assuming all of your staff are honest.

Very little research has been carried out in relation to the reasons why white collar crime such as embezzlement and fraud occurs. This is about to change however in light of the increasing number of cases of white collar crime.

Statistics show however that women are much more likely to be caught and arrested for embezzlement than men. Without a solid base of research to work from, it is very hard to understand what motivates more women to embezzle and rationalise or justify such unethical behaviour.

There are theories that suggest that many women (and indeed men) who embezzle genuinely need extra money due to financial or personal problems that they face and this behaviour is often justified when the embezzler convinces themselves that they will pay the money back in some way shape or form in the future.

It is probably safe to suggest that women who embezzle are more likely to carry out the crime to satisfy the needs of others such as their children. Their intentions in many cases may be well meaning if the money, assets or property is embezzled with a view for instance to put food on the table at home - or to provide a good life for their children.

Embezzlers usually have no previous convictions. After all, they are all in gainful and meaningful employment. Instead they may simply feel guilty at work, being away from their families and in turn pilfer, albeit illegally, in an effort to meet the needs of their family.

In other cases, it is clear that many embezzlers have gambling problems, shopping addictions or other addictions brought on by emotional or relationship problems that require money. It is fair to say that those in this addiction category are far more likely to slip up and get caught. It is likely that embezzlers in this category keep stealing until they either are treated for their issue or get caught red handed.

Many embezzlers who are caught in the act claim that what they did was an honest mistake. As an employer you must consider what the employee is attempting to achieve by claiming ignorance to their misgivings.

While they claim that an unfortunate event or a series of unfortunate events was an honest mistake, the reality is that they may be attempting to garner sympathy and reduce the seriousness of their honest mistake.

Perhaps it is worth asking an employee who presents with this explanation, after employee fraud is detected, what has landed them in a situation where they have to resort to stealing from the very employer that pays their wages. While all staff may have the best intentions, not all can resist the temptation to take advantage of an opportunity when it presents itself.

Mistake #8. Encouraging a culture of embezzlement in your organisation

It is incredibly important to look from the top down when approaching issues related to embezzlement, company culture and fraud deterrence.

Where there is an obvious culture of either honesty, dishonesty or entitlement amongst senior management in a company or organisation, this sentiment filters down and either impacts an organisation positively or negatively in a huge way.

A poor company culture at the top simply encourages an environment where it is impossible to go against the boss. How can a company that behaves unethically at the top entrust their staff with assets and expect those staff to act ethically themselves when handling these assets?

Many employees who are placed in a company where there is a culture of entitlement become jaded to the point where they genuinely feel or believe that they are entitled to certain property or assets themselves in the course of their work.

Another type of embezzlement is where an employee with access to company belongings or stock on hand thieves and takes the items in question with no intention to return the said items to the employer. A theft by employees in this instance may be an isolated/solitary event or employees may make a habit of taking many goods on a regular without permission over a prolonged period of time.

Employees in the retail trade may develop a habit of walking off with merchandise if proper security policies and protocols such as random searches are not put in place. This problem is so prevalent in the industry that some of the world's leading retail outfits build a contingency into their mark-up to cover this shrinkage. In many cases where stock or property is taken, the act is rather brazen and it is often found that the behaviour of other employees influences the behaviour of subsequent thieves.

The more the theft or pilfering of items such as stock or property occurs in a workplace, the more this behaviour is accepted within a group of peers. It's reasonable to suggest that groups of employees in certain circumstances work together to create a system of theft that is perceived to not have any impact on the company or organisation in question. In some cases if an employee resists this culture of thieving and pilferage, that employee may be rejected or bullied inadvertently by their wider group of workplace peers.

Mistake #9. Thinking small time embezzlement isn't a big deal

What is clear is that theft, corruption and embezzlement is rampant in companies of all shapes and sizes. Businesses in Europe lose millions if not billions of euro annually due to embezzlement.

Similarly, across the pond in the USA the problem appears to be just as bad.

Both the Association of Certified Fraud Examiners and the security and investigations firm Marquet International have carried out surveys and studies in an effort to quantify the scale of embezzlement in developed countries. Here are some of their findings:

- The average loss caused embezzlement was $140,000 in cases that went to court.
- More than one-fifth of embezzlement cases in the USA that were investigated and went to court totaled at least $1 million.
- Nearly half of small businesses do not recover any of the fraud related losses, even after a case of embezzlement is detected.

- The size of the embezzlement loss is often related to the position that the embezzler holds. This means that if the embezzler is in a position of significant authority they will likely embezzle more money than that of an employee with less power and control.

- Most embezzlers are first-time offenders with clean employment histories.

- Occupational fraud generally lasts about 18 months before being detected.

- Most companies do not usually have good fraud detection systems and most embezzlement is detected through employee tips and whistleblowers.

Traditionally, organisations do not want the bad press or perceived reputational damage that comes with being an easy target. Traditionally matters related to employee fraud and embezzlement were handled internally or the perpetrator was quietly show the door.

However in recent years as organisations become more tuned in with the economic losses associated with embezzlement and as they realise how rampant embezzlement is, their attitude has changed and they are more likely to seek a prosecution - even if that means they brand name will be dragged through the courts.

Companies are now taking this hard-line approach as they understand that embezzlement will affect their business in at least a few of the following ways:

Cash Flow: Often said, Revenue is vanity, profit is sanity and cash is king. If an employee is embezzling money or stock from a business, this will first and foremost impact revenues. Whether sales have been diverted or profits have been taken at the end of the shift, the bottom line is that the business will not have the reserves it deserves at the end of the day, due to the dishonest behaviour of the employee(s). A lack of cash flow means less jobs for others and less opportunities in the future as cash resources are squeezed, and growth is stunted as significant capital investment requires cash flow.

Operations: Losses due to embezzlement can actually result in the complete failure of a business. Most businesses can't absorb the strain that comes with constant and recurring theft or pilferage - and even at the best of times. Most companies require a constant line of credit to keep operations going. It's safe to assume that many of the company closures and liquidations that we hear about are as a result of documented or undiscovered embezzlement. Many companies who participate in government or public tenders must declare it if one of their employees have been found guilty of embezzlement. This further acts as an operational hurdle and hurts the business.

Brand Damage: Something that we touched on earlier was embezzlement and the role it can play in damaging a company or organisation's reputation. If the public's perception of a brand drops - so will the sales for that brand. This is especially true in the case of companies and organisations operating in the medical or financial space where trust is a cornerstone of their business. No company that's interested in growing value or producing profit wants to be associated with criminality or theft - full stop.

Social Impact: When a business suffers a serious loss through embezzlement, in most cases they must find a way and means of recouping that said loss. This can often come in the form of other employees in the company group being made redundant which has a negative effect on the local economy as a whole.

Lawsuits: One of the most concerning things about embezzlement and the impact it can have on a business is the fact that employees are ultimately the responsibility of the business. In the case of an employee defrauding a customer of the business they work in, it is still the company who will ultimately be brought to court and sued for damages by the customer. Naturally there are ways for businesses to protect themselves in this respect, using procurement software as an example, - but it's often something that businesses overlook.

Mistake #10. Not spotting key cash-skimming signs.

Embezzlement and cash skimming is a huge threat to companies - but especially to cash businesses where it's hard to keep track of inventory and stock. When an employee skims cash from a business they essentially give the customer a good for free and pocket payment for the good themselves. Very often this also involves failing take a record of the sale and failing to open the cash register or provide a receipt to the paying customer when the sale occurs.

The key issue with cash skimming is that it is incredibly hard to detect, as so many people in a predominantly cash business handle cash. Similarly, there is usually no paper trail or sales invoice to substantiate any losses or underperformance.

In many cases employees start skimming by taking cash for themselves with the intention of paying the cash back at a later date. They might be behind on their rent or saving up for a long-haul holiday while paying childcare costs as a single mother. Any employee who handles cash is in a position to skim. This includes sales staff, bank staff, credit union cashiers, waiters and parking officers.

It's very often the most honest employees who are found to defraud a company.

Cash skimming can be tackled by managers who are willing to put in place steps to eliminate embezzlement risk and scrutinise their financial reports. In the case of the coffee shop example at the start of this chapter, it was clearly bad practice to give one person complete control of the till. The owners should have been more hands on and spent a few days at the till themselves each month to get a good idea of how the business was performing.

It's worth bearing in mind that in many cases, instances of cash skimming can be easier to recognise and spot than our above example. Take a grocery shop for instance. Declining inventory levels are much easier to keep track of and a true financial manager will quickly spot it if inventory and sales do not tally.

Employees use a combination of tricks to fool their employer when cash skimming. This can include carrying out a zero rated transaction during a sale to make it appear like a sale is legitimate. On a similar note, employees who can avail of an employee discount may apply their discount for a number of large transactions each week and pocket the difference themselves. This results in a lower sale for the employer, but a nice payout for the employee.

It is the systems you have in place that will help identify cases of cash skimming in your business. Financial managers who are really well tuned into their business or organisation should take steps to ensure for instance that the counting of cash is not left up to one member of staff. They should also run regular and random inventory counts, track and monitor the number of times employees use their staff discount and watch out for large inventory write-offs. Excessive refunds, price adjustments, discounts, voids, and no-sale transactions should be reviewed carefully on an employee-by-employee basis as these transactions may be related to skimming.

Mistake #11. Failing to implement Prevention and Reduction Strategies

So, what can companies and organisations do to help reduce or even eliminate the risk of fraud or embezzlement in their business or organisation?

For a start, it's worth remembering that any fraud or embezzlement usually carries huge risk and ramifications for employees operating on the wrong side of the law. A prosecution that involves fraud or embezzlement usually results in a hefty fine and jail time for the guilty party.

Each country has its own views on embezzlement - but in most cases the penalties are severe. The penalty will often depend on the level of proof as well as the intentions of the person embezzling during the time when the goods, cash or other assets were diverted.

As well as educating staff about the above potential consequences, finance managers can also do the following to reduce the risk of embezzlement occurring in their business:

1. **Maintain a Risk Register and Update Risk Assessments:**

It's really important that companies adjust their risk processes in line with the changes that are happening in their business or industry. Risk assessments should also be adjusted and tailored so that they take into account emerging technologies. By adapting to change and adapting risk assessment policies, there is a great chance that embezzlement can be identified and proven before it becomes and out-of-control issue.

2. **Split staff responsibility wisely:**

It is important in any business that the control of certain high value assets are split between at least two employees without exception. By following this best practice you can ensure that certain activities like the sale of property or the award of a new contract needs more than just one signature of approval. If you can structure your business so that at least two people are needed to carry out fraudulent activity - you are far less likely to be a victim.

3. **Keep improving:**

Most of our clients find that if they can centralise incoming and outgoing cash distribution, payroll and other critical accounting functions, the opportunity to embezzle is greatly reduced. By following this more closely supervised financial model there is less opportunity for theft to occur.

4. **Dishonesty Insurance:**

Embezzlement should always be discouraged in an organisation, as it can do untold damage to a brand's reputation. However employers can cover themselves financially by taking out employee dishonesty insurance. In the event of the company being a victim of fraud, the insurance kicks in and covers the company from financial loss due to employee theft of money, property and other assets. Always remember to fully disclose material facts at company level when purchasing such insurance.

5. **Software Solutions:**

Companies that are particularly vulnerable to fraud, such as financial institutions, given the high level of cash they control and handle take expensive steps to detect embezzlement. By monitoring all transactions using an automated monitoring system, companies can identify anomalies that may be caused by embezzlement. When employees know that transactions are being monitored, they are less likely to take a risk. Remember, to be successful, an embezzler needs access to money with no oversight!

6. **Background checks:**

Conduct background checks on all new employees who will have the opportunity to embezzle when working in your company or organisation.

Embezzlement Checklist

1. Know what embezzlement is.

Make sure you know exactly what is embezzlement and what is not.

Use this knowledge to look out for tell-tale embezzlement signs.

Make sure your staff know that you will not tolerate embezzlement.

2. Watch the Payroll Department

Cross reference bank details with employee names.

Protect your organisation by putting safeguards in place.

Centralise or outsource payroll management and tasks.

3. Keep your eyes open

Spot unusual profit trends. Report anything that doesn't look right.

Keep good records and tabs on expenditure

Petty cash going missing is a warning sign

4. Accept that Embezzlement is rife!

Remember that your staff and employees are human.

Don't make it easy for embezzlers. It's your responsibility to close loopholes.

Avoid giving any staff member ultimate responsibility.

5. Start with education

Encourage tip-offs by educating staff about the impact of embezzlement.

Make sure staff know what behaviour is acceptable and not acceptable.

Show your staff how easy it is to report embezzlement in your organisation.

6. Perform Background checks

Take the time to screen and qualify job applicants.

Look for false information on CVs.

Check for staff convictions on a regular basis.

Accept that any staff member can embezzle.

7. Even your closest staff can embezzle.

Gambling problems and shopping addictions can all lead to embezzlement.

When you spot embezzlement, ask yourself if there is really such a thing as an honest mistake.

8. Tackle cultural issues in the organisation.

Management must lead by example.

Watch staff who display a sense of entitlement.

Remember that the embezzlement of company stock/items is just as bad as cash theft.

9. Keep telling yourself that embezzlement IS a big deal.

Remember that embezzlement is hurting your bottom line and impacting performance.

Embezzlement can hurt your brand and damage your firm's reputation.

10. Pay special attention to cash-skimming.

Split your staff responsibilities wisely.

Use software solutions to identify anomalies.

Reduce cash handling as much as possible.

Suppliers

Lumos, an emergency lighting company based in Bristol, manufactures a range of fittings and fixtures for the construction industry. Many of the components they use in the manufacturing of their emergency lighting are systems brought in from China.

Thanks to the quality detection systems they had in place, management at Lumos discovered that the number of defective imported parts per container load was rising to the point that it was at an unacceptable level. It turned out that one of their main China based suppliers were ignoring agreed standards and were supplying faulty components.

As an importer of components, management knew that they had a responsibility to ensure that defective parts did not enter the market - especially when it came to their range of health and safety products.

They approached the supplier with their concerns and what followed was a stalemate situation. The supplier rejected all suggestion that the parts being supplied were not up to the required standard and Lumos had to cancel payments for container shipments which were already en-route to their manufacturing facility. This resulted in a shortage of certain components that were used in the manufacturing of the emergency lighting products.

Upon termination of the contract it appeared that the chinese manufacturer were happy to cut ties with Lumos. In hindsight, one particular negotiator at Lumos had cut an incredible deal with the supplier - a deal that at the time seemed too good to be true.

Lumos had been working with the chinese supplier for over two years and although some efforts such as sample ordering were taken to mitigate risk at the commencement of the contract, no real quality checks were ever carried out. On a similar note, no close relationships or ties were developed between the staff at Lumos and the staff at the chinese operation. Management at Lumos were naive enough to think that by simply telling the supplier of their requirements - they were guaranteed to receive components of a good and consistent quality for an indefinite amount of time.

This case demonstrates that if left unchecked, suppliers may choose to deliberately ignore quality for various reasons. Companies and businesses can be left in impossible situation where a supplier rejects quality issues and refuses to work around a supply issue or quality problem. This leaves a company at great risk.

Clearly, in the case of Lumos, their chinese component suppliers did not have a history of quality management and did not follow quality assurance best practices. That said, Lumos were guilty in this case of taking their supplier for granted, which had a detrimental effect on the relationship.

Lumos were lucky as they were able to identify a new supplier who had the ability to flex their operations to accommodate them at short notice. If it wasn't for this they would have had a serious supply issue.

Needless to say, things were done very differently the second time 'round. Lumos were sure to provide their new supplier with step-by-step manufacturing procedure documents, so that they could be sure that the supplier would deliver the components according to their specifications.

Management at Lumos travelled to China in an effort to break down cultural barriers and build trust with the new supplier. Management had learnt the hard way and now appreciated the level of attention to detail that is required when ordering from a supplier in another district or country. What followed was months of project management and quality checks - to ensure that all aspects of the production process got the seal of approval.

The good news is that Lumos were incredibly lucky and the experience they had acted as a catalyst for improvement. This chain of events has been instrumental in helping them become a stronger and more adaptable company.

The incident completely changed the way Lumos does business. Now, before launching a new product their product team work closely with potential suppliers of components by overseeing the initial tooling themselves. New suppliers are always asked to build fully functional prototype samples for a fixed fee before being awarded any contract. After that, appropriate risk profiles, control plans, work instructions, and inspection plans are put in place for every supply project. This provides the supplier with a step-by-step and detailed set of manufacturing processes for each component they supply. On the other side, weekly conference calls and regular check-ins give Lumos peace of mind.

Realising the importance of suppliers and the impact they can have on a business has revolutionised Lumos' business. Going forward the company plan to develop a supplier quality program whereby their own in-house product specialists will spend physical time at each supplier's facility in an effort to help suppliers learn and apply manufacturing guidelines correctly.

Not only will this increase the speed of supplier adoption, but it will also increase supplier retention and improve the overall flow of data and communication between their company and the companies that supply them with components. Lumos can already see that the steps they have taken to put best practice systems in place has set solid performance expectations. Cases of quality/recall issues have plummeted. Today over 99% of their supplies pass the stringent quality standards they demand.

Chapter Summary

In this section we will be exploring the many different reasons why companies and firms should develop supplier relationships, even in cases where there appears at first glance to be no need to.

Developing solid relationships takes time, and you don't want to be forced to settle for what's available at short notice when a problem arises.

Suppliers should be strategic partners, able to provide the materials and parts you need when you need them. Choosing the best supply chain partners from the outset will save you significant time and money in the long run.

Mistake #1: Neglecting Supplier Relationships.

Suppliers are a vital element of any business and they play an important role in enabling stakeholders of all shapes and sizes to benefit and make gains from the business. It's becoming more and more widely accepted that companies should aim to commit to ethical and responsible business practices when it comes to dealing with their suppliers. Similarly, a company's chosen suppliers should operate in an ethical and legal manner that is well aligned with the ethos and purpose of the company they are supplying goods or services to.

For every company that is doing meaningful business, whether they are involved in the manufacturing of goods or not, it's incredibly important that they develop and nurture good relationships with their suppliers. Suppliers are a cornerstone of every business and without raw and finished supplies, businesses would simply find it impossible to grow.

It's worth noting that many of the supplies that companies procure are non-manufacturing related supplies, such as the procurement of stationery or the procurement of services such as connectivity and internet related services. With this in mind, suppliers in many cases provide crucial supports to businesses - such as market intelligence, advice on materials, industry insight, strategic opportunities and consultative feedback.

Businesses that want to win in the long run should consider their suppliers as strategic stakeholders in their business. After all, businesses that can build a meaningful relationship with their suppliers go on to achieve cost reductions, opportunities to better develop their product offering and chances to push sales at strategic times during the year in partnership with their supplier.

Businesses that fail to approach supplier selection with the same approach as a human resources department approaches the hiring process are making a critical mistake that will likely cost them dearly.

Typically we break suppliers down into the following categories:

Producers and Manufacturers:

Businesses involved in the resale of goods buy low cost raw materials or components through a manufacturer. The typical manufacturer will have a client-side salesperson who they can build a close relationship with. Many manufacturers will require a high order volume per unit.

Wholesalers:

Wholesalers operate using a distribution model - by buying directly from manufacturers in bulk and then selling the raw materials or components on to smaller businesses. Dealing with a wholesale distributor can be more costly than dealing directly with a manufacturer - though the wholesaler will often supply materials and components from a wide selection of manufacturers, and sell these units in small quantities.

Niche Producers:

Exclusive distribution of unique creations is frequently offered by independent craftspeople who sell through reps or at trade shows.

Ultimately, everyone in business wants to get the most value from their suppliers - but it's important to keep suppliers on your side too, as your business also depends on your suppliers. Without great relationships with your suppliers, you can't serve your customers properly.

Mistake #2: Failing to set KPIs for Suppliers:

A supplier procurement KPI is a measurable value that tracks all relevant aspects of a suppliers performance when providing goods and services.

The existence of KPIs enable financial managers and procurement departments to control supplier performance with a view to improving efficiencies and optimising the sourcing of goods and materials.

Here are a few of the most critical suppliers KPIs that should be set in your organisation and tracked on a continuous basis.

Set standards for suppliers:

You need to always make sure that suppliers broadly fulfill your requirement. A company should lay down a set of standards for suppliers and these standards should be met at all times. This applies to everything from delivery time to supplier discounts and offers.

Purchase Order Sign-Off:

Procurement managers should set timeline KPIs when it comes to internal staff and suppliers signing off on purchase orders. There are so many steps to the purchasing process from initial purchase order creation to order approval, receipt, invoice and finally, payment of the order.

Availability of Stock:

You should always set KPIs in relation to the suppliers ability to cater for urgent stock demands. Using this KPI you can track the number of times that goods were not available from your supplier.

Defect tracking:

It's important to keep tabs on the quality of the materials, components or goods that your suppliers supply your business with. This KPI is necessary in determining the quality of the materials that are going into your products.

When it comes to the goods you sell, your reputation is on the line as a procurement manager and if some of the components you are using have defects this could result in product recalls or bad publicity for your company further down the line. This KPI is especially important in high risk industries such as the automotive or pharmaceutical industry for instance.

Time Taken to Fill Orders:

Companies should measure the amount of time it takes for suppliers to fulfill an order from time of ordering. By tracking this KPI over time you may be able to identify issues in the production or administrative stages that can be worked on and improved.

For each raw material or component that you buy on a regular basis, you should set a target amount of days under which the lead time should stay. If you see that your supplier repeatedly fails to meet this target over time, measures should be taken.

The Real Cost of Procurement:

Companies should have a good idea of how much it costs for each purchase order that is raised in the company. In reality, the cost of processing a purchase order can include many administrative variables including manual labour and account management.

Cost Reduction Successes:

If your team or department are achieving hard savings through their work as procurement professionals - these savings should be recorded. For suppliers that have been servicing your company for many years, you can compare last year's costs with this years costs to see if any like for like cost reductions have been achieved.

Cost Reduction KPIs:

Suppliers should be encouraged to reduce potential future costs and make savings where appropriate without reducing the quality of the good or service being delivered.

Mistake #3: Forgetting to carry out proper supplier evaluation

It's important that you know what to look for when selecting suppliers that will provide benefit to your business. Too often, companies do not spend enough time evaluating their suppliers, resulting in expensive mistakes. Never be afraid to ask potential suppliers a few probing questions when evaluating them, as it's in their interest to demonstrate their ability to work with your team.

Suppliers should be evaluated under the following areas before being selected:

Communication:

Whether it's a delivery issue or a quality issue, mistakes happen. A good supplier should always be there for you when you are faced with a problem. By getting suppliers to commit to a service level agreement you can get a good idea of how hands on they are when it comes to communication.

Remember that as a procurement manager you can also take proactive steps to encourage communication. Before committing to working with a supplier make sure that they are happy to have regular conference calls with your team on a regular basis. Setting a regular slot in everyone's diary gives you time to discuss and plan strategic objectives together for everyone's benefit.

Track Record:

You can check a supplier's track record by asking for customer testimonials or case studies to be made available to you. What you are hoping to see from this is that the supplier can demonstrate a consistent level of quality work with businesses of a similar size and nature to your own.

Much of this information may already be available on the website of the supplier. If you have the opportunity to jump on a call with a few previous clients of the supplier it may be worthwhile asking them why their relationship with the supplier ended.

Capacity and Scope:

If you're thinking big, you probably want to deal with a supplier who can stick with you for years to come as you expand and grow your business. You know the importance of keeping your demanding customers happy and maintaining satisfaction means asking suppliers questions relating to their ability to handle large orders quickly.

If demand for your product or services spike, you want to be working with a supplier who can help you meet the demand that's there without question. Volatility in customer demand can have a negative effect on your productivity, so it's important to find a supplier that understands this.

Commitment:

You should clearly set your minimum requirements when it comes to actively engaging with a supplier. It is then up to the supplier to prove that they can meet these requirements, or demonstrate a commitment to improve any unacceptable lower standards within a reasonable timescale.

For assurance you may also request a commitment letter from a supplier which should set out in writing that they will deliver to your company's requirements, regardless of the needs of their other customers. One top tip is to look out for suppliers that have quality marks or internationally recognised certification standards.

Supply Chain Control:

It's worth evaluating your suppliers from a supply chain control point of view. Ask yourself if the supplier themselves are reliant on other businesses or other factors. Can they always deliver goods or services, or will there be times when they will be waiting on another supplier in order to fulfil their contract to your business?

It's always necessary to consider the flow of goods and services before settling on one supplier in particular. Suppliers should take steps to deliver your goods or services in as efficient and economical a way as possible.

Finances:

A supplier can only deliver on their promise if they are in a financially sound position themselves. Supplier turnover levels should be screened so that you can be sure that they are a large enough outfit themselves to manage the project well and address any issues if a problem occurs.

The financial account details for most registered companies are publicly available for a small fee. You can also request a tax clearance certificate from suppliers to ensure they are tax compliant.

Pricing:

The pricing of goods and services is ultimately just one of the factors to consider when choosing suppliers. Suppliers have to pay for materials and/or labor in order to deliver the goods or service to your business. Suppliers want to recoup their direct costs and add a markup to cover indirect costs and profit.

It's always advisable to shop around to get an indication of the price you should be paying for any high value good or service. If your preferred supplier's markup is too high you can buy the goods or services elsewhere.

By carrying out research you may be able to cut a deal with a supplier so that they match or beat their competitors' price. Some suppliers believe that the higher something is priced, the more likely that it will be perceived as a higher quality product or service.

Consistency:

In gauging whether the supplier can consistently provide a great service and high quality goods, it's worth examining the relationship between the supplier and their long-standing clients and customers.

Do these long standing customers have a good corporate reputation and do they have complete trust in the supplier? If the supplier has been doing business with a well regarded client for a long period of time it's usually a very good sign.

Supplier Culture:

Choosing a supplier with an ethos and culture that fits in with your that of your own organisation is a critical factor when driving your business forward. If you can see eye to eye with a supplier in this respect it means that the relationships between your staff and the staff of your supplier can form faster.

Better relationships mean that projects take off sooner, with less cost and scope creep. A well matched supplier with shared values is more likely to work closely with you by identifying common opportunities, proposing interesting ideas, and being more eager to make improvements without having to be told to. All of these factors have a positive effect on your bottom line.

Sustainability:

With climate change concerns growing internationally, you want to work with a supplier that strives to improve people's lives. Their business focus should extend beyond their products, services and profits. It's important for your brand image that you use suppliers that provide a safe working environment for their own workers, and work in an environmentally sound way. Transparency is key here and suppliers should be asked about the sustainability programs and steps they take to protect the environment.

Mistake #4: Paying the wrong supplier:

Negotiations with your suppliers can often fail and relationships can break down over time for many reasons. This can ultimately result in a change in supplier, which in itself is a complicated process that presents many challenges, not least in the confusion this creates when it comes to making payments.

One particular challenge that companies face after undergoing such a change is aligning their accounts department during the transition period so that only the correct invoice amounts are paid to the correct outgoing and incoming suppliers.

If you or one of the people on your team do transfer funds to the wrong supplier, this is unfortunately something that cannot be easily reversed. Great care should be taken in such circumstances and steps should be taken so that the erroneous transaction can be cancelled. For a start, if you know the person or company that the payment was mistakenly transferred to, you should contact them immediately and explain the situation and be clear that you are requesting that they return the funds immediately. It is worth sending this request to them in writing.

Companies that discover that they have paid the wrong supplier or person should also immediately contact their bank and inform them of the payment that was made in error. Banks cannot reverse payments that have already been made, but by letting your bank know that there is a problem, you are encouraging your bank to take whatever steps necessary to give you the best chance of getting your firm’s money back in good time.

If it is apparent to your bank that you made a genuine mistake in transferring funds they will take action and contact the bank that the transfer was made to, asking that the money received in error isn’t spent. While there is no guarantee that your money will be returned setting these events in motion will demonstrate your company’s willingness to fight for the money that was sent in error. The steps you follow from the start of such an unfortunate situation can be used as evidence at a later date if your request is refused or challenged in a court of law.

In any case, once you report the error to your bank and once they relay the message to the bank of the recipient, it is then up to that recipient’s bank to chase their customers and inform them of the matter. If ultimately the company or person that you accidentally sent the money to refuses to return the money things get a little complicated.

Where this occurs, the onus is then placed on you and your company to prove that the money that was transferred to the recipient is not rightfully their money to keep. This is an incredibly challenging task - and one that can drain resources to the point where depending on the sum involved, some may argue chasing the money is not worth it.

What makes things so difficult in the case of accidentally paying a previous supplier is that it can be very hard to prove that the money transferred was not owed to the supplier when they have such a long history of doing business with your firm.

What can make matters even more complicated are cases where the recipient no longer has the money in their bank account as they may have withdrawn it or spent it all.

Take these steps when paying supplier to reduce the risk of this happening to your and your team:

- Bank account details and all large transactions of over $10,000 should be triple checked by your team to reduce the chances of payment going to the wrong supplier.

- All purchase orders should go through a vigorous approval process requiring multiple signatures. Naturally, emails and invoices should accompany all said purchase orders, so that it is clear who should be paid for the supply of the goods or services.

- If you have a very large sum of money to send to a new supplier, as a test it's worth sending a smaller sum first as a deposit and ask them to confirm receipt of this deposit.

- The bank account details of all active suppliers in your company should be reviewed and verified on a regular bi-annual basis.

- By using payment references and online tools such as IBAN checkers, your team can increase their chances of spotting and identifying payment errors.

Mistake #5: Failing to understand the importance of supplier negotiation:

Dealing with suppliers really puts your negotiation skills to the test. Negotiation is a two way process and a key part of this process is getting to know your suppliers better.

Knowledge is power in the negotiations game and by understanding how much a supplier needs a contract for instance or by identifying how much added value and expertise a supplier brings to the table, should enable you to be able to make better choices when it comes to drafting and agreeing contract terms.

When it comes to setting terms there should always be compromise from both parties. If compromise and trust does not exist then you should seriously consider your options and ask whether the supplier in question is the right fit for your organisation.

Before pricing negotiations begin you should take the time to work closely with the supplier in clearly identifying what your priorities are as a customer. Make it clear to the supplier which aspects of the service are most important to you (non-negotiable aspects) and which aspects are of less important in your line of business (negotiable aspects). For example, in some industries fast delivery times will be far more important than the colour of the item being supplied for instance.

When you're cutting a deal with a supplier it's vitally important that the deal must appeal to both parties. If you get greedy and push a supplier too far this could jeopardise your relationship with the supplier and they may refuse to deal with you or your firm. Business must consider the consequences and cost implications in the breakdown of such a relationship unexpectedly. There are many hidden costs associated with replacing or changing suppliers, especially if the change occurs during a busy time of the year for your business or if the change results in a change in technology and ordering systems.

Play fair by following these tips, and always only agree to terms that suits your needs.

- Focus on the positives by letting suppliers know which parts of an agreement you are happy with and then follow on to outline which parts of the contract you feel can be improved.

- Have a concrete idea of what discounts or improved terms you feel would be acceptable. Too often we come across people who enter the negotiation process without actually knowing what they want to achieve from it.

- Never show your cards too early by suggesting that you are willing to make a compromise. It's inadvisable to give anything away for free at the start of the negotiation process.

- Before starting negotiations, consider and make yourself aware of negotiation tactics that the supplier may use.

- When it comes to successful negotiations, an honest and confident approach usually works best.

- Never ever accept the first offer that's brought to the table.

- If the price agreed is too low to be true, there's probably a reason for this. You should do your own due diligence and investigate what corners may have been cut to allow such a low price to be offered.

- When it comes to services, always ask for a custom price. By removing some features that you don't need from a service you may be able to agree a reduced price.

Mistake #6: Not benchmarking suppliers.

Something that we encourage in the purchasing and procurement space is the benchmarking of suppliers. This involves evaluating and comparing the performance of your suppliers as well as comparing them with the suppliers that your competition work with.

The real challenge when it comes to benchmarking of any sort is finding the data and information to carry out accurate industry comparisons and supplier comparisons.

Some industries are very transparent when it comes to the release of information and you may be aware of competitors that have a clear advantage when it comes to their profit margins, product delivery times, product defect rates or the cost of goods per unit sold. The worry is that these successful competitors may be working with suppliers that are more efficient or committed than your very own suppliers. That is why continuous competitor analysis is essential to the continued success of your business.

In the case that your company lacks meaty insider knowledge relating to your competition, it is still possible in most cases to gain a reasonable insight into your competitors business practices, processes and performance - to see how they are performing. A good place to start is in analysing how your competitors bring prototypes and products to market, take note of the investments being made in research and development.

It's also advisable to take note of how your competitor's new products or services are developed and how your competitor goes about meeting a customer’s order or respond to sales inquiries. This allows you to gather valuable insights and gives you an indication of how you stack up in comparison to competitors.

Within the procurement context, supplier benchmarking can be of considerable value to companies. If we apply the same investigative and reach oriented approach as above with our own suppliers operations in mind, we can gather some idea of how reliable the supplier will likely be over a period of time. This can be done by identifying and communicating benchmarks to suppliers that relate to critical needs within the business.

By carrying out a benchmarking exercise you can categorise suppliers by persona and rate your suppliers based on the risks that they bring to the table and the unique threats that they pose to your business and it’s operations. While the collection of this data and categorisation of suppliers may appear futile to some, it is your expectations as a business owner and client of the supplier that should in an idea world dictate the behaviour of your suppliers.

Supplier benchmarking also heavily depends upon the availability of information. Much of the necessary information should be readily available to you given that most suppliers are established companies that file public records on a yearly or bi-yearly basis.

Remember, a lot of the data that you need when benchmarking a supplier is at your fingertips. For example, your accounts department should be able to provide you with information relating to company suppliers, including details of the value of contracts that the supplier holds with your company. Similarly, they should have details of which departments in your company use which supplier most frequently and provide an idea of the number of competing tenders or quotations that were received for each project that was won by a particular supplier.

Critical benchmarking questions to ask yourself about a supplier:

- What public information is available about your suppliers?

- Can you find out anything about your supply overall approach to customer service?
- Is the supplier ISO certified?
- What trade associations have accredited the supplier?
- What is the average number of years of service of employees with the supplier?
- What is the average rate of employee turnover in the suppliers business?
- What are the five largest customers of the supplier and what industry are they in?
- How long has the supplier been in business?
- How do the prices quoted by the supplier compare against market prices?

In order to draw accurate comparisons and generate an accurate supplier benchmark, many suppliers must be benchmarked and the results must be amalgamated and displayed using a survey research tool.

The result is a collection of data which allows your company to identify suppliers who are customer focussed, suppliers who are price focussed, suppliers who operate with clients in your industry etc. This valuable data means that you are free to approach suppliers and provide them with feedback which in turn allows them to address their shortcomings. It is only through supplier feedback that a company can give suppliers a clear set of expectations which lead to an improvement in existing performance and the reduction of risk in the future.

Mistake #7: Failing to recognise a good supplier.

Most companies only think about price when it comes to evaluating their suppliers. While the price of materials and services is important, it's also worth remembering that other factors such as quality, responsiveness and reliability matter just as much to businesses that wish to succeed.

Whether it's obvious or not, your business relies on many suppliers to succeed. If in the long term a supplier can help your business to sell more products, maintain customer satisfaction or reach new customers then you should want your suppliers to do well, even if this means paying a fair or premium price for goods or services.

Good suppliers must be reliable:

The suppliers you work with should be able to consistently provide materials, goods and services that are of a high standard over a long and extended period of time. In doing so, trusted suppliers are helping you and your business to satisfy your customer's needs in the long term.

Good suppliers must offer quality goods and services:

Established and reputable suppliers can usually demonstrate their ability to provide consistently good quality materials, components and services through well defined standard operation procedures and production practices that they are willing to share with their customers. To a degree, customer testimonials and social reviews can also give you an indication of supplier quality.

Good suppliers invest in next generation safe equipment

Working with suppliers that have the latest technology and equipment means that there is less likelihood of downtime and supply disruption. Suppliers who invest in better machinery can produce more materials in less time and carry out services quickly with minimal disruption to your business. This applies to everything from manufacturing equipment to the delivery vehicles that your suppliers use to deliver products and services to your business.

Good suppliers carry out independent research and product development.

You want a supplier that is ahead of the curve and interested in moving in an upwards trajectory with you. Suppliers who constantly challenge norms and push out the boat by making improvements to the components and materials they produce or supply are much sought after. Remember, much independent research must be carried out by the supplier in order for them to understand what the market wants - and a huge part of this research process involves them talking to their own customers.

Good suppliers are in a location that suits your business.

A supplier must have a distribution hub that is close to your business premises, or at least have a reliable transport connection/partner so that they can deliver the goods quickly and on-demand. Similarly, distribution hubs must be located in regions where economic, political and environmental factors will not inhibit production or delivery.

Good suppliers are established players.

You'll want to work with a supplier that has been in business for at least a few years. Suppliers that have long-term relationships with other firms are usually a more promising fit than suppliers that are just starting out. You want a partner that's in it for the long haul. In the event of a disruption in supply or a quality problem it's much easier to deal with a company that has a number of senior executives on hand to help.

Mistake #8: Not implementing quality systems.

No matter what industry or business you operate in, maintaining a good working relationship with suppliers that you can trust should be a priority.

The number of businesses that go for the lowest price supplier or the supplier with the quickest delivery - without checking out other supplier factors - is remarkable! In many cases this oversight can lead to the delivery of inferior supplies, incorrect supplies or the inconsistent supply of products and materials.

In a world that is becoming smaller and smaller but busier and busier, it has never been more important to work with suppliers who share your goals. If you are not in constant contact with your main suppliers on a regular basis you may have a problem that you're not even aware of.

As a finance manager, you can start addressing supplier concerns in your business or organisation by implementing quality systems taking the time to analyse suppliers on a regular basis. This is the first step towards better working relationships with suppliers.

An example of a quality system to follow:

1. Do procedures exist for all manufacturing activities?

2. Are all processing and inspection steps clearly defined?

3. Are there controls in place to guarantee that only the most current software can be used when machining?

4. Is a maintenance schedule followed for all tooling?

5. Is tool life measured?

6. Are steps taken to prevent environmental contaminants in the manufacturing area?

7. Are there any safety issues that might impact the production process?

By implementing supplier quality systems, whether automated or manual, you can:

- Lower defect rates. There is a general expectation in manufacturing industries that the supplier defect rate should be less than 25 PPM or 0.0025 %.

- Eliminate supplier non-conformance by ensuring that suppliers are kept within arms-reach at all times and by maintaining communication.

Supplier Checklist

1. Value Supplier Relationships

Work on building and improving your relationships with suppliers.

Lean on suppliers for market intelligence, advice on materials and industry insight.

Make it worthwhile for suppliers to do business with your organisation.

2. Set Supplier KPIs

Lay down a set of standards for suppliers.

Measure the amount of time it takes for suppliers to fulfill an order

Track product defects and recalls.

3. Perform Supplier Evaluation

Consider a supplier’s track record.

Choose a supplier with similar growth aspirations as yours.

Choose suppliers that can prove that they can sustain supply levels.

4. Be wary of paying the wrong supplier

Send a smaller sum before making a large deposit, and ask the supplier to confirm receipt.

All large transactions should be triple checked by your team.

If a payment mistake occurs, notify your own bank immediately.

5. Put thought into your negotiation strategy.

Never ever accept the first offer that's brought to the table.

Try and achieve compromise from both parties/sides.

Have a good idea of what discounts or improved terms you feel would be acceptable.

6. Benchmark your Suppliers

Start by looking at your main competitors and the suppliers they use.

Look for accreditations and social proof.

Categorise suppliers based on price/quality/service etc.

7. Recognise a great supplier

Value reliability

Value good quality

Value suppliers that invest in ideas and the future.

8. Implement quality systems.

Suppliers with shared goals should be preferred suppliers.

Perform quality inspections at the supplier's facility.

Agree and document safety and quality procedures with the supplier.

Contracts

Examples of good and bad contract management are all around us. Ultimately contract management comes down to accurately weighing up risk and efficiency. Businesses must make sure that they give themselves adequate time to learn the particulars of the contracts they enter or create and how elements of the contract can impact their business in its current financial and operational state.

One interesting contract case that we have come across involves a coach hire company purchasing a range of new buses in an effort to expand the business. The stock buses were to be converted into luxury buses at the time of purchase as part of a strategic move to enter an emerging market.

In an effort to house the new buses a new parking and service facility had to be built in the coach hire company's yard and IT infrastructure was needed to manage their growing fleet.

Management did not think carefully enough about the scope of the contract and job at hand. The entire project (including the IT infrastructure element) was awarded to a building contractor.

Ultimately not enough attention was paid to the IT element of the project at the contract development stage and it was eventually found that the building contractor was not in any way qualified to take on this task. It was too late however as contracts had been signed and the building contractor was fully compliant with the contract terms.

Throughout the entire contract management process, many major details were missed because the wrong people were involved at the wrong time. Those who had the expertise that was required were left out of the loop, resulting astronomical additional costs that resulted in the entire project being shelved.

Case outcome summary:

When it came to it, we found that the coach hire company had failed to involve their own IT team in reviewing the contract that was awarded to the building firm. When it was discovered that the building firm was not qualified, major changes to the scope of the project were made in an attempt to remedy the situation - but this only resulted in increased costs and increased project timelines. The building firm's lack of expertise in the area of IT remained the same.

When the relationship between the building firm and the coach hire company inevitable turned sour, the project manager was found to have lost his copy of the original signed contract. No copies or digital records were kept. The building firm abandoned the project and this caused such disruption that finding a suitable replacement was not practical. In the end all of the new fleet was sold at an auction by the company in a last ditch effort to stem the massive losses due to the project over run. The vehicles had hefty outstanding loan payments and a strategic decision was made to terminate the project.

Chapter Summary

In this section we will be exploring the importance of putting time and thought into managing contracts. Broadly speaking, contracts should follow the SMART methodology. Contracts should be specific, measurable, achievable, results-oriented, and time-constrained.

You should focus on ensuring that the contracts that you are involved in have a clear duration, well defined quality specifications and a focus on cost effectiveness.

Mistake #1: Renewing contracts without adequate review:

When a contract expires and it's up for renewal, too many businesses blindly sign along the dotted line without reviewing the contract terms.

We all know that in business an awful lot can change in very little time. That's why each and every contract should be reviewed before being renewed - period. This ensures that changes that have occurred in the business since the older contract was agreed are taken into account.

Bear in mind that every contract needs to be reviewed by someone who has a good eye for detail and preferably a legal background. All individuals involved in the management and negotiation of the contract should be focussed on achieving an agreed/desired outcome for the business.

Remember, each and every contract you sign has legal ramifications for your business - so that's why it's incredibly important you understand what you are signing. Here are a few things to consider when reviewing a contract:

1. **Always Negotiate:**

It's important to remember that the terms in every contract are moveable. Ask yourself what elements of the contract are most important to you and always ask for more. Your suppliers in most cases expect you to negotiate, so they will always incorporate a little wriggle room into initial contract proposals. A good place to start when it comes to negotiation is to talk to the person who will be dealing with the supplier most and ask if there is anything they would like to change or modify to make their own job easier.

2. **Formalise Names:**

Make sure that all parties involved in the contract are clearly named on the contract. To avoid any ambiguity or confusion, the names of the companies involved and their registered business addresses should be clearly listed on the contract.

3. **Don't leave blanks:**

If you leave a blank section on a contract there is potential for it to be filled out at a later date by someone else that's not on your side. Make sure to sanity check your contract document for empty blank spaces and put a line (with signature initials) through any blank spaces that you cannot complete.

4. **Consider each parties obligations:**

A contract essentially outlines a series of obligations and responsibilities. A good contract review involves extracting the obligations of each supplier and analysing these obligations on their own in an effort to ascertain whether a fair deal is being agreed. If you can extract this data and put it onto a spreadsheet, you and your team can better understand the contract terms. This document can also in turn become useful at a later date when the contract is being executed.

5. **Stay Safe:**

In a world of GDPR and data security. It's vitally important that you consider any data sharing stipulations around the contract in question. Also consider commercially sensitive information that is mentioned in the contract and ask your supplier that the contract remains confidential and protected. This is one document that you don't want to fall into the hands of your competitors.

6. **Disputes and Termination:**

Always include a dispute process in the contract and make sure that there is a get out clause of some sort to allow your business an early exit from the contract if required.

Mistake #2: Allowing Scope Creep to occur:

Scope creep is where so many changes are made in a project to the point that it spirals out of control. The project grows and certain elements that were never included in the original brief start becoming requirements. This leads to a disorganised project that in most cases fails to achieve its original objectives and aims. Contracts have an important part to play in reducing the chances of scope creep occurring.

Managers and employees alike in your organisation need to understand how important it is to review key project factors such as time, budget and other resources made available to them for the project they are working on. By understanding these factors, they are in a better position to detect and manage scope creep.

The best way to prevent scope creep from happening is to understand what can cause scope creep. In most cases scope creep occurs when the project at hand is not well planned out and controlled. Confusion over small things at the planning stage that are not swiftly addressed can grow in time to become bigger issues. If for instance a manager does not specify his or her exact technical requirements to a contractor, there may be differences in expectations which ultimately cause delays and arguments down the line.

Managers must have full control over the project at all times. This means that only approved team members should be allowed to make changes to the direction of the project. Project management software can help with the approval and permission elements of any project.

Something else that should be paid close attention to is risk. Before the commencement of any project… and before the project is rolled out, key risks associated with the project should be documented and solutions proposed as a safeguard. Anything that could result in a change of plan should be evaluated as a risk.

By setting clear and realistic objectives you can significantly decrease the risk of scope creep setting in. Without clear objectives, miscommunications and misunderstandings can destroy the project at hand. Most successful projects are only successful because there is a good manager working in the background to ensure that the team is working together and keeping the lines of communication open.

In general scope creep results in a painfully disorganised project that increases costs for all parties involved and leads to operational delays.

While we would advise organisations to take steps to avoid allowing scope creep to set in - there is also a thinking that in some cases, scope creep can actually be of benefit to a business from a product development perspective. While the scope creep may result in increased project costs and delays - it can also be seen as simply “part of the journey” towards creating a great and well tested product.

It can't be denied that with the more time that's spent on a project - more and more learnings and discoveries are made.

Our tips to avoid scope creep would include constantly reviewing the status and progress of a project so that external and internal objectives are clear. It's all about communication and identifying issues and problems before they have enough impact to change the course of a project.

To avoid scope creep - bear the following in mind when writing and developing contracts:

- Agree solid milestones, deliverables and budget.
- Use project management software and tools.
- Demand regular reports from your staff/contractors.
- Agree timeframes and report work that is running over time.
- De-construct large volumes of work so that it is in bitesize chunks that are more manageable.

Mistake #3: Poor digital recordkeeping:

In the procurement space it's essential that contracts are held safe and secure for the duration of the contract and even after the contract expires. Contracts are important as they document the work that is to be carried out and can be used to solve disputes and in general can be used to clarify questions over service level requirements and expectations.

When it comes to the public sector, adequate contract record keeping is even more important. These records show that a fair and transparent competition was held and can be used as evidence when this is disputed by tender applicants that were unsuccessful in the award of a public tender.

Businesses that don't keep digital copies of all contracts and agreements are missing a trick. While it is understandable that having a tangible paper version of a document is strangely satisfying, digital record keeping systems make it much easier and efficient to capture, store and share information at the touch of a button.

One of the key advantages to keeping digital records is that contract reports can be produced instantly so that procurement managers can see in a flash how many contracts are active within the company at any one given time, and the particulars of each contract can be analysed on the fly.

By keeping a digital record of all contracts:

- You can see all income and expenses related to that particular contract.
- Keeping digital contracts requires less physical space. Signed contract copies can be taken off-site by a records management agency.
- Contract copies can be made with ease, unlike printed copies which require individual page scanning.
- Contracts (historic and current) can easily be found and referenced.

When it comes to contracts and their role in maintaining a healthy flow of cash, electronic contracting can help. With electronic records there is much less chance of mistakes like missing signatures occuring - as the contract can't be shared for approval without all mandatory signature fields being filled.

Digital contracts also have no chance of getting lost in the post as they are sent via secure email. You don't want to have to ask a potential client for a second signature after closing a deal. The more problems that your clients and customers encounter with the contract they are signing only results in more opportunity for them to reconsider their investment and back out of a deal.

Because electronic contracts can be sent via email, they can be reviewed and approved much faster. This means that money is paid for products and services much quicker so that the company has more cash to cover essential staffing and sales costs.

If as a business all of your contracts are still in paper format - you're operating in the dark ages. Customers are now comfortable with e-contracts and they are aware of how quick and easy they are to sign on an iPad or from their desktop using a third party document signing software.

Mistake #4: Not planning ahead before the end of a contractual relationship:

All companies, both on the receiving and purchasing end of a contract, should anticipate and plan in advance the particulars of what happens when the contract or legal agreement comes to an end.

The truth of it is that the end of any contractual relationship can cause disruption to management, staff and customers. You must plan ahead of time in order to protect your business.

There are several things to consider and plan for before a contract comes to an end. Naturally, the larger and more significant the contract in question, the greater an impact its completion can have on a business. Crucial things to consider include whether the service that is being supported through the contract needs to be continued by some other means, whether the current supplier will hold some level of IP in relation to the work they carried out after the contract ends, how their knowledge will be transferred over to a new supplier and how the changeover will impact staff and budgets going forward.

Here's a list of things to consider when supplier succession planning and planning for contractual change:

- Is there scope for the current contract holder to be awarded the next contract.
- Is there a transition period required or already in place?

- In cases of a specialised service/product delivery, could the introduction of a new supplier result in a temporary or sustained reduction in service quality?

- Does the termination of the relationship have to be kept quiet for brand or operational reasons.

- Does the old supplier have to hand back any data, software or equipment to your organisation?

- Does the supplier have a responsibility to destroy any documentation or sensitive data such as tooling plans or customer information? This is especially relevant in the cases where the supplier was dropshipping goods direct to the customer.

- Make sure that it is clearly stated who owns any intellectual property that the supplier was involved in creating or using during the contract period. This should ideally be established from the outset of the contract.

- Ask the supplier to hand over a full list of quality and control records in relation to the project they were working on. This includes data, procedures, accident reports, access logs, error logs, etc. This information will be helpful in the onboarding of a new supplier and can be invaluable in the case of a product recall or quality issue further on down the line.

- If the supplier is being asked to leave the contract early and outside of the contract terms - you need to know how much compensation is due to be paid as a result. In some cases this compensation payment can be written off against fees already paid for services which were never delivered or still to be delivered.

When the contract does end - it’s worth reviewing the successes and failures of the contract. Here, you can evaluate how the supplier performed and try and extract key learnings which can be used in the future when you or your team executes similar contracts in the future.

Mistake #5: Setting or agreeing to misguided contract terms:

When drafting up a contract or legal agreement, one must take great care to use words that accurately convey the desired meaning. Even small mistakes and misleading phrases can result in a contract becoming redundant and not worth the paper it's written on.

Much of our communication in everyday life is 'implied' communication. When it comes to the law however there is no room for businesses and individuals to leave themselves open to being challenged legally.

Over generations, a huge range of words and phrases that are tied to proven legal concepts and laws have been developed by people in the legal profession and if you don't express something exactly as intended in a contract a loophole is created. In essence, some of the language used in contracts can be confusing and hard to understand for good reason.

That said, this doesn't mean that it's simply OK for anyone to create contracts that are deliberately misleading and convoluted. Very often misleading and convoluted contracts are not legal. A contract can only be deemed to be valid if each party accepted the terms of the said contract. How can one accept the terms of the contract if they did not understand them in the first place?

The important thing is being able to differentiate between contracts that are excessively long/convoluted and contracts that are actually genuine contracts that are written in a way to safeguard the issuing company or organisation.

As a general rule of thumb, if you are signing a contract, you should never sign it if it contains language or phraseology that you don't understand - without having a solicitor or other legal expert review and explain the contract in full to you.

Mistake #6: Leaving contract review and changes up to the legal department alone.

While it might seem strange at first, offloading contract review work to the “non-legal” members of your team can be hugely beneficial.

Involving various staff members in different functions and positions within your company to this area has a number of advantages. While legal experts have a great eye for detail - nothing beats listening to people at the coal face of the organisation. These individuals bring a fountain of knowledge to the table during contract reviews and negotiations as they have hands on experience.

By involving staff members across various functions in the contract review process, you can lean on them in order to better understand how workflows and system operations might be improved in the future.

From a human resources and staff empowerment point of view, research shows us that when employees feel valued and empowered at work, job performance and job satisfaction increases. By involving staff in the contract review and decision process you are effectively telling them that their opinion and input is valued.

By all means, staff with a legal background and your in-house or external legal team are still crucial in maintaining control and mitigating risk when it comes to reviewing and signing off on new contracts - but by also involving staff at all levels you can enter a new contract fully informed.

When working with a number of teams or staff members in reviewing a contract and agreeing changes or needs, it’s vitally important to take control of the project from the outset by providing the people who are involved with a structure to follow. This might for instance involve creating a survey for the relevant staff to complete in an effort to understand more about problems and pains that they currently experience on a day to day basis.

It is important that everyone involved in the review and suggestion stage is on the same page and involved to the same degree as one another.

Try and capture feedback that takes into account the following:

- Ways your staff feel their tasks can be streamlined.
- Learn more about admin tasks that are time-consuming.
- Identify strengths and weaknesses in the relevant team.
- Ask staff about what they would like in an ideal world.

With the right direction, and by asking the right questions you can gather valuable insights and contributions that can be taken into consideration and result in positive changes to the contract specification.

By delegating out some of the contract specific review process, the time of high value legal staff/contractors can be put to better use - on issues and activities that are more pressing and important for your organisation.

Consider the other benefits that this approach brings:

Better Work Balance:

Many of your staff members are probably unmotivated and feel like their job never changes. By offering them work that is different and new to them, their interest is sparked and your organisation will be a more attractive place to work.

More Chance of spotting errors:

By putting more eyes on a project it's more likely that you will spot mistakes and the contract review process will be significantly sped up. This will result in an increase in operational efficiency as the contract can be executed sooner rather than later. By assigning some contract review and management responsibilities to the right people in your organisation, your company will become more efficient and productive.

Mistake #7: Failing to automate the contract process.

In this mistake we point out the benefits of automation. If you haven't automated your contract processes - you need to start thinking about it.

By automating the contract process from start to finish your business can without a doubt grow at a faster pace. Similarily, life is made easier for everyone in your finance department when the contract process is automated.

Automating the contract process effectively helps to drive value and reduce risks. Read on to find out exactly how automating can have this positive affect.

Your contracts and team will be more organised.

Being able to find and reference contracts may seem like an obvious element to contract management. However, many of our clients and organisations that we talk to every day have no way of managing this.

If your active contracts are hidden among thousands of emails, or stashed in a drawer under books and piles of paper, you will need to spend time trying to find them in the case of something going wrong or something needing to be reviewed.

On a similar note, storing contracts in an organised manner using spreadsheets can also present issues as links (file paths) to specific files over many years becoming corrupt.

To put it quite simply, being able to access and keep track of your contracts in both urgent and non-urgent circumstances is crucial for productivity and reducing risk.

By embracing automation and using contract specific software you can store and find your contracts straight away on a dedicated cloud-based server, with all contracts organised by type, category or project.

Security Fears are reduced.

With the advent of GDPR in Europe and many privacy and data hacking incidents in the USA, it has never been more important to ensure that data security is taken seriously.

Unauthorised contract access and privacy breaches are a reality in 2019. Businesses should take careful steps to ensure that sensitive contract documents relating to commercial agreements and supplier information does not fall into the wrong hands.

Think of all of the information that is on even the most standard of contracts. Everything from sensitive data, identifiable information, trade secrets and bank details regularly features on commercial contracts.

It's never been more important to guard these documents. By automating your complete contract management process you can store, share and make changes to contracts in a secure environment that has security features built into its core.

Regardless of what contract is added to the platform, it will be fully protected and safe from prying eyes. To add to this, your employees don't need to worry about treating certain contracts differently to others.

Automation also means you don't forget about your obligations. Financial managers need to be great timekeepers - especially when it comes to contracts!

By failing to renew and review contracts for instance, your company can lose out on opportunities and loose suppliers to competitors that operate in the same market.

On a similar note, if you discover that you have to review and renew a contract at short notice you may be forced into agreeing unfavourable contract terms in order to simply secure a deal and maintain supply of a critical service or component.

Through automation of your contract process you can forget about having to remember when a contract is due for review or renewal.

Automatic reminders can be set up for each individual contract and you can work through an on-line checklist to ensure that you are meeting all of the predefined obligations your company has set against the contract in question.

When a company reaches a certain size, not automating processes can lead to significant roadblocks that stand in the way of getting things done. By spending time on finding and setting up a system that works for you and your business - you can fully automate your contract related tasks and reduce risk in your business.

Mistake #8: Having too many active contracts:

A major focus in most procurement and finance departments today is the consolidation of suppliers. This brings huge advantages when it comes to contract management as it means that your company can focus less on administration and more on product quality and growth.

If your business has hundreds or thousands of suppliers it becomes very difficult to manage all of these suppliers. By categorising suppliers into different groupings and segments you may be able to take steps to reduce the number of suppliers without compromising service level.

Take for instance a company with a premises that has active contracts with a pest control company, a security company, a cleaning company, a catering company and a maintenance company. By shopping around they are sure to be able to find a single facilities management company with a specialised team that can instead manage all of these services from under one roof. Even if this facilities management company outsource some of their operations - the contract (and all associated admin including billing) will still remain with one company.

So, why is it better to have fewer suppliers in some cases?

- **Staff Cost Savings:** Fewer suppliers means less resources being pumped into supplier/contract management. Why should you have your highly paid staff run around in circles managing and reviewing multiple contracts when one supplier can manage all elements of the contract. Over time this can represent huge savings in staff costs.

- **Time savings:** On a similar note, by working with just one supplier, less time has to be spent on communications between your team and suppliers. Fewer employee hours spent on contract management means more time spent on other important tasks.

- **Economies of scale:** Suppliers commanding larger contracts can often offer greater discounts. This in turn results in better buying power as you will likely be working with a larger supplier that is better connected in their industry and more willing to give your business bulk discounts.

- **Improved efficiency:** Working with a plethora of suppliers is hard work. If you're working to tight deadlines and timelines, you can improve the time it takes to get a job done and reduce the time it takes to launch new products, innovations and improvements to your business.

- **Reduced Training:** Suppliers all use different systems and platforms to manage their own businesses. If you're working with less suppliers it's easier to train your staff on only a handful of supplier systems.

- **Clarity:** When a problem arises, it's easier to see which supplier is causing the problem. You can get the answers you need quicker - without having to link in with dozens of suppliers to find the root cause of a problem.

- **Better integration:** When it comes to providers utilising the services of various technology providers - it's better to use one platform that lives under one login. This way, there are less compatibility or integration issues which may lead to system breakdowns and endless software patching.

Supplier consolidation is so important as it results in cost and time savings. You are effectively eliminating the hours spent managing a range of suppliers and putting this value back into the business.

Mistake #9: Reviewing Contracts Too Late:

Many businesses and financial controllers are so busy that they only remember to review and analyse expiring/renewing contracts at the last minute - when it's too late.

As covered earlier in this chapter, there are various automation tools that can be used to set reminders for you and your staff when it comes to expiring contracts.

In this brief section we will outline the most important stages of the contract review and approval stages. These guidelines should help you understand the amount of time and thought that each significant contract should be given.

Planning & Preparation Stage. (6 - 12 months before)

In the planning and preparation stage you have an opportunity to draft up sample contracts and pass them by suppliers in an effort to collect feedback.

By doing this well in advance of when you need the supply of a service or product, you can hold meaningful negotiations to ensure success later on in the process.

During this time you will also have ample time to set up policies and procedures for the management of the contract.

Pre-Contract Stage. (3 - 6 months before)

Now that negotiations are complete or at least in the advanced stages, you have to give yourself and your team time to review the agreed terms.

This is a time to go over everything with a fine tooth comb and check for errors and omissions that could put your organisation at risk.

By spreading all contract decisions over an extended period of time, you can ensure that time is taken to fully optimise and customise contracts so they fit the exacting needs of your organisation. This allows you to full compare, analyse and critically evaluate potential suppliers before signing along the dotted line. The start of the contract review process should take place at least 6-12 months before the contract is due to start or be renewed.

Contracts Checklist

1. Only renew contracts after an internal review

Negotiate at every renewal as standard.

Clearly define each parties obligations.

Make sure there is a get out clause of some sort in the contract.

2. Beware of Scope Creep

Agree solid milestones, deliverables and budget.

Use project management software and tools.

Demand regular reports from your staff/contractors.

3. Keep better digital records

Analyse all income and expenses related to a contract.

Encourage customers to start using e-contracts.

4. Planning ahead before the end of a contractual relationship

Consider the business case/need for a new contract term.

Consider the learning curve required for new suppliers.

Make sure the outgoing supplier hands over any project related records

5. Avoid misleading contract terms

Only work with contracts that use the correct verbiage.

Never sign a contract if it contains language that you don't understand

Make sure there is a get out clause of some sort in the contract.

6. Involve multiple departments in the contract renewal process

Nothing beats listening to people at the coal face of the organisation.

People who are involved feel that their opinion and input is valued.

By asking the right questions you can gather valuable insights from your staff

7. Automate the contract process

Automation means easier to reference contracts.

Automation results in reduced security risks.

Automation involve trigger based reminders.

8. Avoid having too many active contracts

Less supplier management means less administration.

The more business you do with one supplier, the better discounts you are eligible for.

Less suppliers means less systems you and your staff have to use and learn.

Negotiation

Trust. Its a word with a big meaning. Measuring someones can be an accolade or an attack. It can be the start of a great relationship or bring about bitter recriminations at the end of one.

Who do you trust your boss, your colleagues, your spouse?

What do you trust, the news, social media, youtubers?

Trust is important for both business and personal life but when it comes to negotiation it is key. In this chapter we will look at the three elements of trust and the five ways you can make significant increases to your margin using negotiation, but first a true story.

5 to 1 on a big loss

For a time I worked for a large multinational company in the facility management business. This company had large pharmaceutical customers as well as banks and other blue chip businesses. These companies paid us so they could outsource the management of their buildings, security, cleaning and canteen as it was not a core part of their business.

As the Irish part of a huge multinational we tended to get signed up to deals that had been agreed in Europe or the UK. So the customer would have buildings throughout Europe and invariable, due to the Irish low tax rates, they would have something in Ireland. These are the buildings we would then get to manage.

In 2016 we got tagged onto one of these large contracts. It was to manage a large number of stores for a massive gambling company throughout Ireland and Britain. The contract started and I was the accountant on the numbers. Month one we lost some money...OK, early days I thought lets see how it goes. Month two we lost more money, “emm, not sure where this is heading I said at the meetings”, knowing exactly where it was headed. On that one contract worth millions we lost minimum of USD50,000 per month, every month.

There was no option but for me to do a deep dive on the contract, the numbers and ever detail to get to the bottom of these losses. What

I found was amazing. This negotiation and contract was a master class in how NOT to do business.

Location

The British part of the business had done all the talks and discussions with the customer, even though over 50% of their shops where located in Ireland. When going through the details the British had only looked at the location of their shops which of course where located mostly in medium sized towns. The Irish locations were completely different. While the British engineers could head out to a town service the shop and then go onto another client the Irish engineers, because of Ireland is more rural, had to head to places that contained a betting shop with no other clients in the area. This had significant cost impact on the Irish accounts.

Suppliers

When the contract was being priced up the sales people contacts some potential partners and got costings off them for delivering services which we could not deliver. One of these was waste collection. The problem was when discussing the requirements with these suppliers they “forgot” to mention the frequency of the collections and the location of the shops. When they had signed the deal with the customer and gone back to the waste collection company with the exact details they were quickly told that they could not deliver the required service levels at the estimated price.

Specialty

The contract required specialist skills in a number of areas which we could mostly sub contract, but one stood out, security and fire alarms. To be able to install, maintain or even wire up an alarm you need specialist training and certification. None of our employees had this training. It cost €895 per person to get certified.

Incredibly all these areas had been missed by the sales team. They had neglected to ask the operations team what they could deliver and therefore they had no **red lines**. They hadn’t bothered to accurately calculate the cost of delivery and so had no idea of what their **walk**

away revenue figure should have been. Finally they had not engaged other potential customers in the market so they have no **BATNA**.

Bottom line was that they were going to do a deal with that customer, for anything they wanted, at any price.

Crazy.

Having worked through the figures I quickly realised that we were destined to lose USD600k to USD700k on this deal per annum. It was unsustainable.

Once I presented my findings the senior management it was decided that they would head over to London to discuss the deal and its implications with the British part of our company. Sadly for all of us they came back empty handed and we ended up losing a huge amount of money on that one contract.

This really eroded any teamwork, collaboration and most importantly trust between the two parts of the business.

In the next section we explore the parts that make up trust and why it is so important in business.

Three Elements of Trust

There are three parts to trusting someone. Everyone can always name the first one but the other two are just as important if you wish to believe what the person is telling you.

Honesty

This is the one point we all immediately think of when we first consider trustworthiness or not of a person. Are they telling us the truth, is there another agenda, what is really motivating them and how can I find out? This is clearly an issue and something we need to pay attention to but it is not the only factor and it can be hard to quantify. In practice the honesty of a person only becomes apparent over a long period of time. It can also be affected by different situations so it can be difficult to know unless you have spent the time getting to know the person in different settings.

Authority

Does the person have the authority to deliver what they have promised? This can seem obvious but consider the times you have "agreed" a deal only to be told "I need to get this signed off by my boss". So important to find out at the start of the negotiation if this person is the right person for you, can they sign off, do they have the budget, are they even in the correct department. Finding this out, known as presales, can save you a lot of time and effort.

Competency

In simple terms can the person you are negotiating with do what they are saying they can do. You are looking to get your business refinanced, you are speaking to the MD of a small financial planning company, so this person has the authority. You have known this person for many years and you believe what they say, so they have honesty. She tells you that she can refinance your business through a complex series of financial products. Now you know she is honest, you know she has the authority, but can she pull off this complex refinancing?

This is the final part of the trust equation. You must weigh each of these up to understand if the person you are speaking with can deliver on the agreed deal.

In my story above you can see how the trust was eroded and really failed to grow back. The only change that made a difference was when one of the managers who was responsible for "winning" this deal left. Then his new replacement had a clean slate and could begin to build back up trust over many months.

1. **Red LInes / BATNA / Walk Away**

The first part of any negotiation is to understand what you want. What is it that you hope to achieve from these talks. It can be money, time, collaboration, service, products or an employee, but it must be clear in your own mind what will constitute a success for you and your business.

Once you understand what will make it a success you can then work out your red lines.

Red lines are parts of an agreement that are essential to you counting it as a success. In short if these are crossed then you have failed to make a good agreement.

Example; you are negotiating the purchase of a business. This business might have a lot of intellectual property. You wish to acquire this as you want to receive the patent fees associated with them. The business seller may just want to sell you the capital equipment, buildings and workforce and instead wants to licence the IP to you and keep receiving the patent fees themselves. Therefore a red line for you is the purchase of the IP along with the rest of the business. If this cannot be achieved you do not want the rest of them business.

Immediately you can see the importance of setting, sticking to and really understanding your red lines. They can be the make and break of a deal. In contract you may have other parts of a deal that you would like, but they are not essential. In fact they are used when negotiating. A key part of any negotiation is to only give away when you get something back.

BATNA means the best alternative to a negotiated agreement. The importance of having this laid our, research and fully understood before dealing begins cannot be overestimated. It is critical as part of your and your team's preparation for an important negotiation to understand what is your BATNA.

Example; your purchasing department is negotiating a new contract to buy tomatoes from Italian supplier. The contract is worth USD10 million. You buy the tomatoes once the harvest is complete. Tomatoes are therefore a commodity and their price will be determined not only by demand but also by supply i.e. how good the harvest is that year. Your team flies to Naples to discuss a possible contract with your supplier from last year. This supplier tells you that the harvest for the year has been poor, and therefore they must increase the price as they have plenty of other buyers for their product. In this scenario if you enter into negotiations with this supplier as your only option then you are limited. Because the product is dependant on the harvest what can you leverage? If it was a component manufacturer and they had invested heavily in new machinery then you could agree to take an increased volume at a lower price. This would work for both of you, utilising his machinery and giving you more products to sell at a better price. With the tomatoes if it has been a bad harvest for one of them then its bad for all. You may get some movement from other supplier but there are usual significant setup and management costs when moving suppliers. In this case you need to have done your research. You know that there may be a lack of supply of tomatoes in the market there are significant amounts of tomato puree left over from the previous year when there was a bumper harvest. Therefore your BATNA is to substitute fresh tomatoes for puree tomatoes in your products. Knowing that buying the fresh tomatoes at the inflated price will mean a higher price which you cannot pass onto your customers you decide to go for the tomato puree option savings the business millions.

Walk away means what is says. Sometimes you are in a place where a deal does not make sense for your or the other participant. In that case you should just walk away. As is often said, the only thing worse than no deal is a bad deal. You may be able to secure a certain ingredient, component or customer but if its not making money you will just spend each month meeting with the management accountant and your boss explaining why you made yet another loss in the month.

2. **Focusing on your own goals rather than on the deal**

You meet the potential customer, supplier, partner and begin your preambles. There is talk of weather, the latest politics and other chit chat.

Finally you get down to business.

Can they deliver what you want, at a price you can pay, during the times you require. This goes on and on and then you notice they are losing interest, they make an excuse and leave.

What went wrong?

By focusing solely on the items you need you have neglected to make it attractive to the potential business partner. They can see that for you to win they must lose. They will have to give up too much at too high a price to make it a deal that is worth their time and effort.

Instead of just focusing on what you want it makes sense to understand what your potential partner requires and then to make a deal that works for both of you. The classic win-win.

Therefore in any meeting where your aim is to make it work long term, it is critical to understand in detail your potential partners position. What would work for them, who do they have to sell it to further up the lin and why is it worth their time to do a deal with your business.

Also part of this idea is building a relationship. Getting to know the potential partner is one of the most important parts of negotiation. You can learn if they are irrational or logical, focused or in disarray, what makes them happy and what annoys them. Using this info you can then make sure to tailor any deal towards their strengths and preferences.

3. Ask for it

Sometimes the simplest and easiest answer can be overlooked. Just ask for what you want. This is particularly important when you are dealing with someone in a different country or culture to your own. Making a very clear statement of what you require to make this deal work for you can give them the necessary information to weigh up if there is potential for a deal to be stuck.

I had my own encounter with straight talking while working in the Netherlands. A German colleague asked me if the accounts were correct for a department within the business. I knew that these particular accounts had been completed by an accountant who was junior and had been coerced into “adjusting” the accounts to reflect figures which made a sales person look better than she actually was.

I tried to explain this to my German collegue, it took me four attempts.

First I told him, “well if it was me I would have a bit more of a look into the numbers to see if they made sense.

He didn’t get it.

Next attempt, “the sales seem a bit high don’t you think?, could they be right…?”

Again it was over his head.

“Sales are too high. Review them carefully. Maybe the numbers are not as accurate as hoped”.

Still nothing. Confused face. I gave it one last try.

“The accountant has inflated the sales numbers to please the sales person on this account. The numbers are incorrect. You will need to revise them.”

Bingo, that got through. He understood. I had learnt an important lesson. Different cultures communicate in different styles and you need to adapt as you see fit.

4. Making Assumptions

The other party wants to make savings, right? They just want to cut the cost or charge you as much as possible and then thats a win for them isn’t it?

Making assumptions without any evidence can lead you into trouble or worse can scupper any hope of a deal. It is important to back up all assumptions with evidence. Doing this will allow you to really understand what is going to work for you and your potential customer or supplier. Falling back on lazy assumptions will only lead you down the wrong road and can mean that you end up fighting of something that neither of you might even care about.

Example of this from real life included a deal I was working on to bring in a new accounting system. At the time we needed to get the system installed, testing and working before our year end. The suppliers of the system wanted to make sure that it worked correctly and that we were happy as they wanted to use us as a reference site.

But as we didn't know what each other wanted we assumed that price / cost was the key and we ended up fighting over this issue.

The solution came when the IT Manager just blurted out in one of the meetings that what was most important to us was that the system was running before September that year. Upon hearing this the suppliers said that was not a problem and they would get stuck in immediately.

5. **Training**

Training your staff is one of the best investments that you can make, but training your buyers will actually make you money. There are of course numerous sales training courses but sending your buyers on a purchasing course will give you big benefits almost immediately.

Think about how much you spend per annum in your cost of sales. What if you could make a 1%, 5% or 10% savings. This would drop straight to your bottom line. Now work out how much that is and compare to the cost of a course for your buyers. This is an annual saving also, not a once off. Every year your company will reap the reward of this saving.

Most courses will cover the following:

- The Importance and relevance of Effective Purchasing
- Preparation of the Scope of Work and Specifications
- The Tender Process
- Selecting the Right Suppliers
- Forming a Contract and its Essential Elements
- Supplier Management throughout the Contract Lifecycle

These should give them the knowledge and skills to:

- Achieve Operational Efficiency in Purchasing

- Select and Managing Suppliers
- Develop a Balanced Performance Measurement Framework that is value driven
- Evaluate Suppliers
- Understand the Stages of Effective Contract and Supplier Management

Always research and check any courses to make sure they align with the business goals and are suitable for your buyers.

Negotiation Checklist

1. Red LInes / BATNA / Walk Away

Discuss and agreed the red lines with the stakeholders.

Agree on leader for the talks.

Research the market for other options.

Agree when a walk away position, which will be reviewed regularly.

2. Focusing on your own goals rather than on the deal

What do the other team want from this deal?

What is a win for the other team?

FInd out who their expectations and importantly the expectations of their supervisors.

3. Ask for it

Understand in detail our company requirements for this deal to be perceived as a success.

Evaluate the chances of this being acceptable to the other team.

Decide when to ask and who should ask.

Make sure to ask the decision maker.

Give them time to respond.

4. Making Assumptions

Do research to support our strategy?

Understand the market as a whole and where we and our potential partners fit into this market.

Is this deal attractive to our partners, if so why? Be specific.